

# STIMULUS OVERSIGHT—2009

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## HEARINGS

BEFORE THE

### COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS UNITED STATES SENATE

OF THE

ONE HUNDRED ELEVENTH CONGRESS

FIRST SESSION

**MARCH 5, 2009**

**FOLLOW THE MONEY: TRANSPARENCY AND ACCOUNTABILITY FOR  
RECOVERY AND REINVESTMENT SPENDING**

**APRIL 2, 2009**

**RECOVERY AND REINVESTMENT SPENDING: IMPLEMENTING A  
BOLD OVERSIGHT STRATEGY**

**APRIL 7, 2009**

**THE AMERICAN RECOVERY AND REINVESTMENT ACT: MAKING THE  
ECONOMIC STIMULUS WORK FOR CONNECTICUT  
FIELD HEARING IN HARTFORD, CONNECTICUT**

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FUNDING**

**SEPTEMBER 10, 2009**

**FOLLOW THE MONEY: AN UPDATE ON STIMULUS SPENDING,  
TRANSPARENCY, AND FRAUD PREVENTION**

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Committee on Homeland Security and Governmental Affairs



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# **FOLLOW THE MONEY: TRANSPARENCY AND ACCOUNTABILITY FOR RECOVERY AND REINVESTMENT SPENDING**

**THURSDAY, MARCH 5, 2009**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 10 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, Pryor, McCaskill, Tester, Burris, Collins, McCain, and Voinovich.

## **OPENING STATEMENT OF CHAIRMAN LIEBERMAN**

Chairman LIEBERMAN. Good morning, and welcome to today's hearing, which we have titled "Follow the Money"—not just "Show me the money," but "Follow the Money: Transparency and Accountability for Recovery and Reinvestment Spending." In other words, what are we going to do to make sure that the \$787 billion—or at least the \$501 billion that we judge will go to spending as opposed to tax reduction, is spent wisely? And how will the Federal Government account for all the money that will be spent over the next 2 years as part of the American Recovery and Reinvestment Act of 2009 (ARRA or Recovery Act)?

It is our Committee's responsibility under our traditional Governmental Affairs role to study "the efficiency, economy, and effectiveness of all agencies and departments of the Government." We take this responsibility seriously, and we intend to ensure that measures are put in place to prevent cost overruns, provide strict oversight of contractor performance, and ensure that grant conditions are met and that fraud is promptly prosecuted in all aspects of the stimulus spending, which is truly unprecedented in the amount of money that Congress has appropriated and in the speed with which we have asked our government to spend it.

I want to thank our witnesses for being here: Robert Nabors, the Deputy Director at the Office of Management and Budget (OMB), whose boss Peter Orszag has told us, will be the man whose hands will be on the stimulus program; Gene Dodaro, the Acting Comptroller General at the Government Accountability Office (GAO); and Phyllis K. Fong, Inspector General at the Department of Agriculture (USDA), but here particularly in her role as Chairman of

the Council of the Inspectors General on Integrity and Efficiency. That is a great title, and you have earned it.

I thank you all for being here today. Each of you have a critical role to play in ensuring that these stimulus funds are spent not just quickly to help our economy, but effectively to protect our taxpayers.

History can be our guide in this. It was actually 76 years ago yesterday that President Franklin Delano Roosevelt began his famed first 100 days with his first inaugural address to a Nation then mired in the Great Depression. Unemployment was around 25 percent, so as bad as things are and as worried as the American people are about their futures, as we all are, it was a lot worse then.

In his address, President Roosevelt told an anxious Nation, "Our greatest primary task is to put people to work. This is no unsolvable problem if we face it wisely and courageously. It can be accomplished in part by direct recruiting by the government itself, treating the task as we would treat the emergency of a war, but at the same time, through this employment, accomplishing greatly needed projects to stimulate and reorganize the use of our natural resources." And that, of course, fits quite perfectly the aim that I think most Members of Congress who voted for the stimulus bill had in our minds.

Ultimately, the New Deal put 8 million Americans back to work and accomplished a lot. Six hundred and fifty thousand miles of road were built. That was an enormous boost to commerce in our country. The Bonneville and Grand Coulee Dams were built that brought electricity into rural homes. Airports, like LaGuardia in New York City, were built, and they became the hubs of a new modern transportation infrastructure. And, of course, thousands of other public buildings and parks were constructed, many of which we still use today.

By the end of President Roosevelt's first term, the unemployment rate had been cut by more than half, and may we be blessed to see a similar cut at the end of President Obama's first term.

The American Recovery and Reinvestment Act is similarly ambitious, seeking to save or create 4 million jobs by putting Americans to work in traditional infrastructure projects like roads, bridges, and buildings, but also by laying the groundwork for a 21st Century economy with investments in clean and renewable energy, high-speed rail, computerized health care records, and expanded broadband access—an information highway across the Nation.

History also shows that the New Deal gives us reason for some caution as we embark on this massive public spending stimulus program, because the fact is that not all the New Deal projects left the grand legacies like those I mentioned a moment ago. For instance, in the Nation's capital, 100 people were hired as part of that stimulus program to scare pigeons. Well, I do not think we need that today, but others may disagree. In New York, people were put to work as fire hydrant decorators. The Federal Government funded a study of the production and efficiency of safety pins.

As I say this, I miss Senator Coburn. I feel that he should be here. [Laughter.]

So frequent were these dubious projects that the word “boondoggle” was born to describe any job or program that wasted money and produced trivial results. In fact, so common was the use of this word that President Roosevelt felt obliged to rebut it. He said in one speech, “If we can boondoggle ourselves out of this Depression, that word is going to be enshrined in the hearts of the American people for years to come.”

But that is not the way it has worked out, really, although we look back at the New Deal programs that got us out of the Depression with great appreciation. Today, there are still boondoggles, and we all know and disdain them. While we understand that our economy needs a real jolt urgently, we want to make sure that every dollar of the \$500 billion that the Recovery Act targets for spending on projects and programs will be used to restart the economy with hopefully not a penny lost, wasted, or stolen.

Again, we understand that speed is important, but we simply cannot repeat the kind of mistakes we have made in other hasty spending projects, such as in Iraq reconstruction or in the aftermath of Hurricane Katrina.

I will say this, and I suppose I am patting Congress and also the Administration on the back: In the American Recovery Act, otherwise known as the stimulus bill, there is some very good language and good provisions to put us in a position to protect the taxpayers in the spending of this money.

First, the legislation includes about \$250 million in new funding for our inspectors general (IGs), who, incidentally, report to our Committee, to hire experienced auditors and investigators and to oversee stimulus spending. I would like to hear this morning about whatever proactive measures are being put together by the IGs to ensure with these new personnel that the stimulus money is spent properly.

Second, the legislation, of course, creates the Recovery Accountability and Transparency Board. President Obama recently chose Earl Devaney, the Inspector General of the Interior Department, to head this board. It will also contain at least 10 other inspectors general from departments and agencies that have jurisdiction over the recovery projects. The board is meant to ensure coordinated and comprehensive oversight of stimulus spending and provide regular reports to Congress and the public. Mr. Devaney is just finding his way through this new responsibility, and we thought it would be premature to have him here this morning. But we look forward to having him testify before the Committee at a hearing quite soon.

Third, the Recovery Act adds protection for whistleblowers who work for State and local governments or for private contractors who generally have no Federal protection against retaliation if they disclose waste or fraud in the spending of these stimulus funds. Of course, some of the most significant information we get about waste and fraud comes from people right in the middle of the system, and they deserve whistleblower protection at all levels.

Fourth, a special Web site called “Recovery.gov” will provide transparency for posting information about spending on these projects.

We want to work closely with the Obama Administration to make sure we have the manpower and systems in place to do the job right and safeguard the public investments. Waste or fraud in the spending of the \$500 billion of stimulus funds will only further erode the American people's confidence in their government just when they and we need them to have that confidence most. That is why our Committee is giving notice with this hearing this morning that we intend to very closely and aggressively monitor spending of stimulus money ourselves and also, if I can put it this way, to oversee those who are given the responsibility by the law to also oversee the stimulus spending, including the three distinguished witnesses we have before us this morning.

Senator Collins.

#### **OPENING STATEMENT OF SENATOR COLLINS**

Senator COLLINS. Thank you, Mr. Chairman.

Over the past year and a half, we have witnessed the collapse of the housing market, the unraveling of our Nation's financial institutions, and the evaporation of trillions of dollars in the stock market and in people's retirement accounts. The financial crisis that started on Wall Street has become a crisis on Main Street in every community in America. Nearly 600,000 Americans lost their jobs in the month of January alone, bringing the total number lost since the end of last summer to 2.5 million. The Nation's unemployment rate is the highest it has been in more than 16 years.

That is why the stimulus bill that we passed a few weeks ago is so critical. The economic stimulus package contains robust infrastructure spending, significant funding for State aid, tax relief for low- and middle-income families, and tax incentives for small businesses. It is projected to save or create an estimated 3.5 million jobs.

The investments in this bill should help to turn our economy around, but to be successful, these stimulus funds have to be spent effectively and with transparency and accountability. They simply cannot be lost to waste, fraud, and mismanagement. As the Chairman has pointed out, if they are, not only will it retard the economic recovery, but it will further depress people's confidence at a time when confidence is needed.

If these funds are not awarded in a timely, transparent, and appropriate manner, the impact of the economic stimulus package will be blunted, and the results, whether for new jobs, better roads and schools, or other critical investments, will fall far short of our expectations. When there is a lack of accountability in Federal funds aimed at stabilizing the economy, goals are not accomplished, and public support evaporates. And, of course, we have only to look at the spending of the Targeted Asset Relief Program (TARP) money to see a cautionary tale.

To avoid the tremendous oversight flaws of the TARP and help to prevent similar abuse in the allocation of stimulus funds, Congress included strong safeguards in the bill. These protections will help to ensure aggressive oversight, enhance transparency, and accountability for taxpayer dollars. The law includes millions of dollars in additional funding for the agency inspectors general and the



GAO, and creates a new Recovery Act Accountability and Transparency Board to coordinate these activities.

I believe one of the most important safeguards is the creation of a new Web site, Recovery.gov, which will allow the public to access information on how the stimulus money is being spent. From my perspective, the more eyes looking at this spending, the better.

Ensuring that the funds are spent properly also requires an efficient and effective acquisition workforce to develop and monitor the stimulus contracts. Federal contract purchases now exceed \$532 billion a year, yet the Federal Government entered the 21st Century with 22 percent fewer Federal civilian acquisition personnel than it had at the start of the 1990s. So what we are going to have is the challenge of a downsized, shrinking acquisition workforce, which is already overwhelmed, coping with an influx of billions of additional dollars. That is an issue I am going to be raising with our witnesses today.

As one of the witnesses who submitted testimony for the record—Allan Burman, a former head of the Office of Federal Procurement Policy—has pointed out, this problem also extends to State and local levels. There is a real question of whether State and local governments are prepared to effectively handle this influx of money and to ensure that competitive processes are followed.

We have learned painful lessons from the Iraq reconstruction and Hurricane Katrina-related contracts that a lack of planning can produce egregious examples of waste and open the door to outright fraud.

Today's hearing will allow us to examine the Administration's plans to safeguard the taxpayers' interests in the economic stimulus plan's effectiveness and efficiency. Our government has an obligation to make sure that these funds are spent wisely to get people back to work, to relieve hardship, and to turn our economy around. America's families, struggling with the economic downturn, deserve no less. Right now I believe that they are hopeful, but they are also skeptical, of whether we can spend this much needed money wisely.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks, Senator Collins. I agree with you on both counts, that the American people, including my constituents that I've talked to at home, really were pleased that we passed the stimulus program. They know they need it. But they are worried about whether we are going to spend it effectively. And that is why I am so glad the three of you are here.

Robert L. Nabors, Deputy Director, Office of Management and Budget, welcome, and we look forward to your testimony now.

**TESTIMONY OF HON. ROBERT L. NABORS II,<sup>1</sup> DEPUTY  
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET**

Mr. NABORS. Thank you, sir. Chairman Lieberman, Ranking Member Collins, distinguished Members of the Committee, thank you very much for inviting me to testify.

We are in a deep recession, which threatens to be more severe than any depression since the Great Depression. More than 3.5

<sup>1</sup>The prepared statement of Mr. Nabors appears in the Appendix on page 181.

million jobs have been lost over the past 13 months, more than at any time since World War II. And the gross domestic product (GDP) declined at an annual rate of 6.2 percent in the fourth quarter of last year—the highest rate in over 25 years. Each community and sector of our economy has been affected, and that is why the President signed the Recovery Act, which is intended to provide relief to millions of struggling families, jump-start our economy, create or save more than 3.5 million jobs over the next 2 years, and steer our Nation out of this economic circumstance that we find ourselves in.

Passing the Act was an important step towards immediate recovery and the restoration of long-term fiscal stability. But for the Recovery Act to be effective, funds need to be spent both wisely and quickly. Allow me to say a few words about the work we are doing to accomplish both of these objectives.

First, for the Recovery Act to have the desired effect, funds must reach recipients quickly. Since the Act was signed, the Administration has been working quickly to channel funding into our struggling economy. Already, more than \$15 billion of Medicaid grant awards have been allocated, covering the first two quarters of fiscal year 2009. In addition, \$10 billion has been allocated to create green jobs, revive housing markets with high rates of foreclosure, and curb homelessness. New funds for unemployment insurance and food stamps, grants to hire more police officers and for workforce development, block grants to States and localities, dam and levee funding, and formula funding for highways and other transit construction have been allocated or will be this month. We are doing our part to expedite this process by working to make our application processes and guidance as clear as possible so that funds reach the hands of those who need them, as quickly as possible. But we need the help of our State and local partners to ensure that Recovery Act funding makes its way into the economy. States cannot let Recovery Act funds sit in “rainy day” accounts, and Recovery Act funds should not be used to reimburse programs for previous expenses.

Second, it is essential that funds be spent wisely at all levels of government and in a way that maintains the confidence of the public. The President understands the magnitude of the government’s responsibility in managing the taxpayers’ dollars. This is precisely why the Recovery Act was designed to ensure unprecedented levels of transparency and accountability, and why the Administration has moved swiftly to implement both the leadership and internal processes necessary to oversee this massive effort.

In terms of leadership, the President designated Vice President Joseph Biden as the Administration’s point person to coordinate the Federal response on the Recovery Act. He has also named Earl Devaney, the Inspector General of the Department of the Interior, as the head of the recovery oversight board.

On process, the day the Recovery Act was signed, the Administration launched Recovery.gov, a Web site that will empower citizens to hold the government accountable by reporting where recovery dollars are going and how the money is going to be spent. The response has been dramatic. Recovery.gov received 3,000 hits per second the moment it was launched, and it has received over 150

million hits since February 17, 2009. As funds make their way to projects, we anticipate that the Web site will be a valuable resource for tracking their use.

In this very early phase of Recovery Act implementation, we are focusing on ensuring that Federal agencies tasked with managing recovery money are executing their mandates well. OMB has transmitted detailed guidance to all of the agencies on how to manage Recovery Act dollars in a way that will promote transparency and efficiency. The guidance calls on agencies to go beyond standard operating procedures and to recognize the unusual nature of recovery funds. Agencies are required to ensure that recovery money is distinguished from other funding in their financial systems, grant and contract writing systems, and reporting systems. For example, within their financial systems, agencies are generally required to set up unique treasury appropriation fund symbols for all Recovery Act funding.

We have emphasized the extraordinary responsibility that falls on all government workers to prove to the American people that we are spending their dollars well. To inform citizens how, when, and where recovery dollars are being spent, the guidance presents new, tight reporting deadlines. This week, agencies began submitting weekly reports that provide a breakdown of funding, noteworthy actions to date, and major planned activities. By no later than May 1, 2009, we have asked that they submit both an "Agency Recovery Plan" and a separate "Recovery Program Plan" for each program named in the Act.

Within OMB, we closely monitor milestones, obstacles, and other significant issues pertaining to the implementation of agency recovery plans on a daily basis, as well as the use of specific funds. We are working to ensure that matters of significance are appropriately brought to the attention of senior Administration officials in a timely fashion so that they can be resolved before problems arise.

However, the Administration cannot achieve the goals of unprecedented transparency and accountability without help from Congress, State, and local governments. All levels of government share responsibly for rooting out error and waste and ensuring that only the most worthy projects receive precious recovery dollars. These projects should meet high standards of economic value and equally high standards when judged by the public for fairness and impartiality.

No one should doubt the importance of the Recovery Act in creating jobs, restoring public confidence in our economy, and putting our Nation back on track. Nor should anyone doubt the importance of implementing this Act as efficiently, transparently, and effectively as possible.

Our success going forward with implementation of the Recovery Act is in large part going to be determined by the tens of thousands of Federal, State, and local officials who will be monitoring this funding on a daily basis. In my work at OMB, I have been very fortunate to have a team of very competent career employees who have been meeting with me on an almost daily basis, and I would like to take this opportunity just to recognize their hard work so far. There are four of them here with me today: Danny Werfel,

David Bortnick, Leslie Field, and Dustin Brown. These four individuals, plus the other individuals back at OMB, should be a model across the Federal Government and across all levels of government in terms of the amount of dedication that they have shown in terms of making sure that this money is spent wisely.

Thank you very much.

Chairman LIEBERMAN. Thanks, Mr. Nabors, and we join you in thanking the people behind you who have helped to put us where we are.

Before we go to Mr. Dodaro, that is a stunning number for hits on the Recovery.gov Web site. That was 150 million.

Mr. NABORS. Yes, sir.

Chairman LIEBERMAN. And that's in basically 2½ weeks—less, actually, since the bill was signed.

Mr. NABORS. Yes, sir.

Chairman LIEBERMAN. Do you have any analysis of what people are looking at? Do you have any sense of who they are?

Mr. NABORS. We are in the process of doing that type of evaluation, but from what we can tell, at least initially, these are people across the country who just want to see how their money is being spent.

Chairman LIEBERMAN. Yes. That is actually thrilling. Or maybe it is intimidating for those who are going to oversee the spending. [Laughter.]

Anyway, that is great to hear.

Gene Dodaro is the Acting Comptroller General, U.S. Government Accountability Office. Thanks for being back here.

**TESTIMONY OF GENE L. DODARO,<sup>1</sup> ACTING COMPTROLLER  
GENERAL, U.S. GOVERNMENT ACCOUNTABILITY OFFICE**

Mr. DODARO. Thank you very much, Mr. Chairman, Senator Collins, Members of the Committee. I am very pleased to be here today to assist you in your oversight of the American Recovery and Reinvestment Act by explaining GAO's plans to meet our responsibilities under the legislation, and also to discuss how we are coordinating with the rest of the oversight entities that are charged with various responsibilities.

The Act gives GAO a range of responsibilities and tasks. They include recurring responsibilities to report and do reviews on a bi-monthly basis on the use of the funds by selected States and localities across the country. We also are charged with reviewing recipient reports, which are required to be filed on a quarterly basis, with particular attention to their reporting of the number of jobs preserved or created.

We also are asked to look at a number of targeted areas: Education incentive grants in particular; the expansion of trade adjustment assistance that is provided; and also efforts by the Small Business Administration to increase lending to small businesses and increase the liquidity in the secondary market for those loans. And we are also tasked with some long-range studies. One includes looking at the impact of downturns on States over the past few decades and trying to develop recommendations going forward for how

<sup>1</sup> The prepared statement of Mr. Dodaro appears in the Appendix on page 185.

the Federal Government can assist States, particularly in the health area, in the Medicaid program, in future economic downturns.

One of the large-scale responsibilities we have is to implement this bi-monthly review of selected States and localities, and we are moving forward in doing that. We have selected 16 States based on expected amounts of money flowing to the States and localities: Population figures, poverty figures, and unemployment rate projections. We are going to track these 16 States, the District of Columbia, and localities over the next 2 to 3 years to have a longitudinal study and analysis of how they have used the money and what the impact has been in achieving the purposes of the Act in these States and localities. These States are expected to receive over two-thirds of the Recovery Act spending, so we believe this will be a really good study and present a national picture.

Now, we are also going to be reviewing the recipient reports filed by all 50 States so that we have information on them, so we will be tracking the activity there. We also will have our Forensic and Special Investigations Unit, which has testified before this Committee several times, do a risk assessment of some of the programs and areas where we would want to do targeted reviews. So just because we will not be in the other 34 States does not mean that we will not do some reviews in targeted areas in those States going forward.

We are in the process of selecting the localities within those jurisdictions going forward, and we will apprise the Committee of the localities that we are selecting within those 16 States.

Now, because a lot of the Federal money will be flowing from the Federal departments and agencies that are under the purview of the inspectors general, who are also going to the States and localities, it is important for us to coordinate our activities with the inspectors general. Soon after the Act was passed, I contacted Ms. Fong, and she and I co-hosted a meeting that involved IGs or their representatives from 17 departments and agencies to begin coordinating our activities. In addition, GAO teams are meeting with each individual inspector general's office to coordinate our activities as they relate to the States and localities going forward.

I have also talked to Mr. Devaney, and I made sure that he understood that we were committed to coordinate with him as he gets the Recovery Board up and running. That will be an important coordination step for us as well.

Similarly, we are doing outreach to the State audit and local audit communities. Through the National Association of State Auditors, Treasurers, and Comptrollers, we arranged a conference call that included representatives from 46 State offices, either the State auditors or their representatives, and we had a similar conference call with local auditors across the country. When we first enter the States and localities, we will be working with these State and local auditors because they understand their localities, and we will be coordinating with them, as well as through the governors' and mayors' offices and their designated representatives.

We also have begun coordination efforts with OMB. Soon after the Act was passed, a number of State officials wrote to Director Peter Orszag and myself about establishing a working group to

work on some of the reporting requirements that were in the law. I talked to Mr. Orszag, and we have begun working with the States and localities on that.

Now, there is one other issue we have brought to OMB's attention and Treasury's attention. As you mentioned, Mr. Chairman, while there is about \$500 billion on the expenditure side, there are also a number of tax provisions that eventually people will want to know whether or not they achieve their objectives. For example, there are recovery bonds. As well as special provisions for depreciation and for creating jobs during this period of time.

Our experience has been at GAO, unless the Internal Revenue Service (IRS) makes a determination up front to collect specific information about the reporting of these tax credits and tax provisions, it will be impossible to determine their effect. OMB and Treasury have responded well to this outreach by GAO, and we are going to be working with them. They are beginning to think about what information should be collected on the tax provisions so that the provisions can be properly evaluated as to whether they achieved their objectives. I think this is very important so that at the end of the period, we will be able to have a comprehensive analysis of the entire Recovery and Reinvestment Act and whether it achieved its purposes.

Also, this early attention up front is really the governing principle and will provide lessons learned about how to prevent fraud, waste, abuse, and mismanagement in these programs. I have listed in our testimony some of the lessons learned documents that GAO has produced in the fraud area: Contract management and competition are essential here; having qualified people, as has been pointed out, is also essential, and I would be happy to talk about that more; and grant management going forward. There are a lot of best practices that are available to the Federal departments and agencies, and I included them in my statement so that they are available at the State and local level as well. We will be meeting with those officials when we enter the States going forward.

So, in summary, I think it is important to have this early outreach. I am pleased to see some of the discussion in the OMB guidance so far. The inspectors general are also outreaching to State and local officials, I think. I am encouraged by that as well. We are going to be doing the same thing at the State and local levels when we enter the 16 States and the District of Columbia going forward.

In closing, I would just say that GAO welcomes the opportunity to help the Congress ensure adequate oversight over this funding. We are committed to meeting our responsibilities on time and in a professional, thorough manner.

Thank you for the opportunity to be here today, and I would be happy to answer questions at the appropriate time. Thank you.

Chairman LIEBERMAN. Thank you, Mr. Dodaro. I find your opening statement to be impressive and encouraging. You have done a lot in a short period of time. You have been proactive, and I appreciate that you are coordinating with the other agencies involved here, both the inspectors general and OMB particularly. I will have questions for you afterward, but thanks for your testimony.

Phyllis Fong, as I said at the outset, is the IG at the Department of Agriculture and Chairman of the Council of IGs. Thank you so much for being here this morning.

**TESTIMONY OF HON. PHYLLIS K. FONG,<sup>1</sup> INSPECTOR GENERAL, U.S. DEPARTMENT OF AGRICULTURE; CHAIR, COUNCIL OF INSPECTORS GENERAL ON INTEGRITY AND EFFICIENCY**

Ms. FONG. Thank you, Mr. Chairman, Senator Collins, and distinguished Members of this Committee. I am very pleased to be here today to talk about the activities of the IG community.

I just want to start out by thanking you and the Members of your Committee and staff for the opportunity to work with you all as the Recovery Act was making its way through Congress. There were a number of provisions that directly affect the IGs, and you have been very helpful in terms of addressing our concerns at an early stage. I want to express our appreciation for all of that.

Chairman LIEBERMAN. You are quite welcome.

Ms. FONG. This morning I want to talk briefly about how the Recovery Act impacts IGs and our responsibilities under the Act and how we are approaching our new responsibilities in a very concrete way.

First off, the Recovery Act gives IGs responsibilities in three areas. We have increased responsibilities for overseeing stimulus expenditures within our agencies. We are now participating on the oversight board, as has been mentioned. And we also have a new responsibility regarding investigations of whistleblower complaints.

With respect to the first area, oversight of agency stimulus programs, we in the community are giving a high priority to this activity. We understand the funds need to be moved out very quickly to address the problems in the economy. We also understand that when funds move out quickly, there is a risk of internal controls not being as strong as they could be. And we understand the need to be proactive.

I want to assure all of you that my colleagues in the community are very aware of the need to be proactive and that all of us are engaged in activities right now to do that. We are also working very closely with GAO and OMB, as has been mentioned by my distinguished colleagues here at the table.

With respect to the oversight board, there were concerns that have been expressed as to whether or not the independence of IGs will be impacted by the creation of this new Recovery Board. I think early on in the process, those concerns were articulated very publicly and in a very articulate way. And we in the community were also concerned initially. But I will say that I appreciate the Committee's help in addressing our concerns, and at this time we do not believe that our independence will be adversely impacted for a number of reasons.

We note that the board's members are now all IGs, and so we would bring to that board our unique perspective and our sensitivity to the need for independence.

<sup>1</sup>The prepared statement of Ms. Fong appears in the Appendix on page 200.

We also note that the chairman is Mr. Devaney, who is a long-standing IG, well regarded in the community, and we know that we can work with him.

And last, but perhaps most important of all, the Act itself provides that the IGs will have the final say as to whether or not we initiate audits or investigations or stop audits or investigations. And so I anticipate that we will be able to forge a very productive working relationship with the board as we move forward, and that we should be able to address any issues that come up.

With respect to whistleblower complaints—you raised that as a new area of responsibility for us—we are very mindful of the fact that whistleblowers deserve protection and are certainly a wonderful source of information for all of us. The Recovery Act gives us, as IGs, some new responsibilities to investigate complaints of reprisal from whistleblowers who are employees of State and local government or non-Federal employers, recipients of stimulus money. This is clearly a new responsibility for us. It is a little early to tell what kinds of issues will arise in terms of our taking on this responsibility. But we are gearing up to do it. We all understand what we need to do, and we will keep the Committee apprised of our progress on this.

Turning to activities that we as IGs have started to undertake to address our responsibilities now, as you mentioned, Mr. Chairman, last fall you passed legislation creating the Council of IGs. We are now up and running. We are an organization of 67 Federal IGs and other senior members of the Administration. One of our main missions is to ensure coordinated approaches to issues that have governmentwide impact. Stimulus oversight would certainly be one of them.

When the Recovery Act was enacted, the Council of IGs decided that we needed to start taking some proactive measures to plan for our oversight activities. And so we put together a working group of the 23 IGs who are receiving dedicated stimulus oversight money, and we have started to share among ourselves best practices for moving forward. We have held some meetings. We have met with GAO. We have talked with Mr. Devaney. And we have started to move out. I want to just highlight for you some of the concrete measures that we are taking now in the community to address funding before the money moves out.

Let me just say that we surveyed the community, and of the 22 IGs who responded, all of them are engaged in proactive measures. These measures range from participating in our agency steering groups and work groups; to identifying unimplemented audit recommendations pertaining to programs that are getting stimulus money and working with our agencies to get those audit recommendations implemented now; to conducting pre-award audits of recipients; and also conducting real-time audits of systems with our agencies; to reviewing agency spending plans for internal controls; to conducting fraud awareness briefings of our departments' employees to make sure that they are aware of red flags that could occur; and to sharing best practices information both among the community members as well as with our departments and agencies.



There are many best practices that we are providing our agency program officials with and saying, look, when you issue grants, these are things that you should be doing right up front.

Probably the key theme that is coming out of the community at this point in terms of proactive work is that there is an essential need for good communication and collaboration with agency program officials. That, in many ways, is really the key to making sure that all of these things get implemented in an effective way.

We also are as a community implementing a number of longer-term measures to provide oversight to stimulus spending, and as you might expect, those would cover a wide range of activities, including sampling of recipients who are receiving funds to make sure that the programs are really operating the way they should be; looking at databases, data analysis; verifying agency data as it is reported to Recovery.gov; handling investigations of fraud; and dealing with whistleblower complaints—all of the risk-based kinds of activities that IGs traditionally do.

The main theme there, of course, is that we as IGs will be looking in our departments to determine which programs are at the most risk or are most vulnerable depending on the money flow and other internal control issues, and then directing our resources to those issues as a priority matter.

Finally, all of my colleagues have indicated that they anticipate challenges in terms of how we meet our oversight responsibilities, and these challenges can range from the very basic challenge of hiring up and recruiting quickly—with our new stimulus oversight funds, we need to recruit more people; that takes some time and effort—to balancing our normal oversight work with other mandated work, and addressing our stimulus responsibilities in a way that we can handle all of the things that we need to do, and do them responsibly.

We also anticipate some issues with respect to data matching. There may be ways to facilitate that process so that we can really identify fraud across agency lines. And I think that is an area for real exploration with the Congress as we move forward.

So in closing I want to say that we are here to do our part. We recognize the need to move out quickly. We are moving out quickly. We look forward to working with you as you identify issues for us to look at.

Thank you very much.

Chairman LIEBERMAN. Thank you, Ms. Fong. Another encouraging report.

We will do 7-minute rounds of questioning. Let me pick up on the end of your testimony because the stimulus bill does give \$250 million in additional funding for inspectors and auditors by the IGs. Do you have any sense of how many people that you need to hire or will want to hire pursuant to that appropriation?

Ms. FONG. Well, the appropriation funds are made to each of the 23 IGs, and they vary in amount. I will say some IGs are getting at the low end of the spectrum perhaps \$1 million or \$2 million.

Chairman LIEBERMAN. Which is for the 2 years.

Ms. FONG. Exactly, for a short period.

Chairman LIEBERMAN. Right.

Ms. FONG. And then at the higher end, there are some of us who are getting \$22 million or \$42 million.

I can speak for myself. At USDA, we are getting about \$22 million. We are looking to hire between 20 and 30 auditors and 10 and 20 investigators. We need some human resource assistance as well in order to staff up and to track our money. And we have already started our recruitment process. It does take some time and effort to do that.

Chairman LIEBERMAN. Yes. So you are beginning basically with the personnel that you have.

Ms. FONG. Exactly right. And so what we find that we are doing is reallocating our audit and investigative resources, taking them off of work that is of lower priority and putting them on our stimulus work.

Chairman LIEBERMAN. Right. Mr. Dodaro, GAO received \$25 million, how are you going to use that money?

Mr. DODARO. We plan to hire up to about a hundred people. Now, the strategy that we have taken here is that we have a lot of former GAO people who have left the workforce, for example, to raise a family. So we have reached out to a lot of people who have left as well as retired GAO employees. We have already identified 65 people who are interested in returning to GAO. Some of them we have actually brought back.

The advantage of this is the money that we have is only available until September 2010, so that you do not want to hire a large permanent number of people.

Chairman LIEBERMAN. Right.

Mr. DODARO. So we plan to fill about half, if not a little bit more of that, with people who have left GAO—and the other advantage is these are people that have already been trained by GAO. They can hit the ground running once we bring them back. This is also something the acquisition community ought to be thinking about doing to help themselves meet this need. But we are doing that, and we also have advertisements out that we have posted for additional help.

Chairman LIEBERMAN. Good.

Mr. DODARO. In the meantime, we are reallocating experienced people to get this up and running. It is important when we go into the States to have experienced people there.

Chairman LIEBERMAN. That is a great idea, a great way to do it.

Mr. Nabors, let me talk a little bit about the pace of getting this money out there because obviously the speed of it is very important. We are trying to fill, as the President has said over and over again, this gap in demand that economists say may be \$1 trillion a year for the next couple of years that is not coming from the private sector.

What are our goals at this point? Let me start with this baseline question. As I recall in the debate here, in the Senate stimulus bill we raised the percentage of money that would be spent in the first 2 years, understanding that in nobody's vision of this could we spend it all within the 2 years. And as I recall, we were close to about 80 percent in the first 2 years of the full stimulus money that would be spent.

Mr. NABORS. As I remember it, the Congressional Budget Office (CBO) estimated that the House bill would spend approximately 60 to 65 percent of the funds within the first 18 months.

Chairman LIEBERMAN. That is right.

Mr. NABORS. And that the Senate bill would spend somewhere between 75 and 80 percent of those funds within the first 18 months.

Chairman LIEBERMAN. Right. That was my recollection, too. So what are your goals from OMB about how much of this money you hope to have out in the economy—and we are talking about the spending side; I am going to get to the taxes in a minute—in the first year?

Mr. NABORS. I do not know that we actually have a particular goal in mind for a dollar amount that would go out in the first year. I think that what we are focused on, especially right now, is making sure that we have a planning process in place so that we are not just throwing money out the door, that we are taking the money that Congress has given us, and we are putting it into those areas that have the highest bang for the buck. And what you will see, especially in the next couple of months, are pretty significant and expedited planning processes within each of the agencies to lay the groundwork so that going into the future we have a baseline by which we can determine how money should be spent, and so that we can expedite that money going into the future.

Chairman LIEBERMAN. Am I correct that on the Recovery.gov Web site you are going to be regularly reporting how much money you have spent of this bill?

Mr. NABORS. Yes, sir. We will be reporting not just the allocation of the funding, but the spending of the funding as it actually goes out.

Chairman LIEBERMAN. We are going to obviously keep in touch on this, but I would be interested, as you go on, to know what your goals are for how much of the money you hope to get out in the first year.

Let me ask about the tax cuts now, the “Make Work Pay” tax cuts, the reduction of the payroll tax. How soon will taxpayers see that so that they will have a little more money which we hope they will spend?

Mr. NABORS. I would want to defer to the Treasury Department, but I believe that they are planning to make that available on an expedited basis.

Chairman LIEBERMAN. OK. Let me go to a different part of this. This goes to fraud. I have two questions.

US-CERT, which is the U.S. Computer Emergency Readiness Team in the Department of Homeland Security, over which we have oversight responsibility, recently reported that it received a bogus e-mail from scammers offering economic stimulus payments in an attempt to steal personal information from those who respond. I wonder if you had heard about that and what you think can be done to warn the public about fraud related to the stimulus package.

Mr. NABORS. I have not heard about that. That causes me great concern, and I would want to go back and talk to—we have a daily conversation with each of the Cabinet agencies, and I think that

this is the type of thing that we bring up to make sure that we have a common way of addressing these types of problems. Obviously, this needs to be dealt with quickly and forcefully to ensure that private information is not stolen.

Chairman LIEBERMAN. Let me ask a final question, because my time is running out, and I will come back on fraud.

The President asked the Vice President to oversee this, so what is the organization chart? Because we have a lot of people involved. We have OMB, we have GAO, we have the IGs, we have the new Recovery Board with Mr. Devaney. Does the reporting all go up to the Vice President?

Mr. NABORS. Well, the way I would view this is that I think it is important that the recovery oversight board and the IGs continue to be thought of as independent. I do not believe that they are actually reporting to the Vice President. They are reporting to the Congress; they are reporting to the American people; they are reporting to the Secretaries. And they are continuing to play the oversight role that Congress has identified for them.

Within the Executive Branch, in terms of the management of the activities and programs, we thought it was important that, to the maximum extent possible, we were coordinated, that agencies were using best practices, that agencies were sharing information about things like contract practices and hiring practices. And the center point for that is the Vice President. The Vice President is the one that calls us all together.

In terms of OMB's role, OMB will continue to play the role that it has traditionally played in both the management and budgetary functions.

Chairman LIEBERMAN. And you have special responsibility there for OMB, as I understand.

Mr. NABORS. Well, the President has asked each agency to designate a single point of contact to ensure that there is clear accountability within each agency. Within OMB, I have been designated as the point of contact.

Chairman LIEBERMAN. All right. That is very helpful. So the Vice President and OMB are basically overseeing the implementation of the stimulus, carrying out of the stimulus act, and the IGs and GAO with the board are doing independent oversight to make sure that the money is being spent efficiently and without fraud.

Mr. NABORS. And in a perfect world, the two pieces are not stovepiped.

Chairman LIEBERMAN. Right.

Mr. NABORS. From our perspective, trying to weed out waste, fraud, and abuse before it actually occurs is incredibly important. It is great to catch the bad guys later, but ensuring that the bad guys do not get the money in the first place is incredibly important, and that is why we have had the initial conversations with GAO, Mr. Devaney, and the IGs ahead of time.

Chairman LIEBERMAN. Good. Mr. Dodaro, I know you want to say something, but I have a lot of Committee Members here, and I am over my time limit. So I am going to yield to Senator Collins.

Senator COLLINS. Thank you.

Mr. Nabors, following up on the statement that you have just made, there is a tension between spending the stimulus money

quickly and ensuring that safeguards to protect against fraud and waste are not suspended. When the government has attempted to distribute funds quickly in the past, we have seen corners cut and protections suspended that have led to widespread fraud. The best example which this Committee uncovered was almost \$1 billion in improper and in some cases fraudulent payments that were made to applicants for assistance in the wake of Hurricane Katrina.

What is OMB doing to ensure that proper controls remain in place despite the need to disburse the stimulus money quickly? What we found in the wake of Hurricane Katrina is that the Federal Emergency Management Agency (FEMA), in an attempt to get the money out to the victims of the storm quickly, suspended all of the internal controls that would have caught applicants that had applied twice, that did not qualify for funding, and in some cases did not live at the addresses that they claimed. That led to literally \$1 billion in improper payments. How are you going to prevent that this time?

Mr. NABORS. Well, I think that there are three things that we are focused on doing. The first, OMB sent out very detailed guidance to the agencies, almost 60 pages worth of guidance, and rather than suspending the normal controls, we actually used the opportunity of sending out the guidance to remind people of the controls that are in place and to remind them of the fact that those controls are in place for a reason—to protect the taxpayers. So as we put out more and more guidance those are the types of things that you will see. Rather than suspending the controls, we are actually reminding people not to suspend the controls.

The second thing is transparency. Both through Recovery.gov and through reporting mechanisms to Congress and to others, we are ensuring unprecedented transparency from the very beginning of the recovery efforts to make sure that we are not in the position 3 months from now where we are asking questions about where the money went.

The third thing that we are doing is we are putting in place very strong planning and reporting processes where the agencies are not just being asked to put out money, but we are asking them to stop for just a brief period of time and think about what are the most effective actions that they could take. And in some instances, those plans will be submitted to the Congress for consultation. In other areas, we will be having informal consultations with the Congress. But I think the more people who can be involved in the types of conversations that we need to have about how the money is going out and where the money is going out, that will help.

And I think the final thing that I would point to is accountability. By putting this information on its web page, on Recovery.gov, by identifying a single point in each agency, we are essentially saying—and I am speaking for myself as one of those people—I am responsible for the actions that OMB take. And when Congress has a problem, when the American people have a problem with actions that have been taken, I am the one that is going to be accountable for that. And I think that combination of activities will help to get at the issues that you have raised.

Senator COLLINS. Thank you.

Mr. Dodaro, the large omnibus appropriations bill that is now before the Senate contains substantial funding increases for many of the same agencies and programs that already are receiving huge funding increases in the stimulus bill. I think it is extremely unfortunate that the omnibus bill has not been revised to take into account the recently appropriated funds in the stimulus bill. That is particularly true for agencies such as the National Endowment for the Arts, the Census, AmeriCorps, and the Department of Agriculture computer upgrades.

Does GAO have concerns that this additional funding, which may well be duplicative and may exceed the entire budget of the agency the year before, will increase the difficulty of ensuring that the funds are spent carefully and well?

Mr. DODARO. We have not been asked to address that issue, so we really have not done the type of analysis to make the comparisons that you cite, Senator Collins. So I am really not in a position to comment on the omnibus as it relates to your questions—we have been focused on the Recovery Act.

But I would say that to the extent to which there can be some flexibilities built into the money that would be beneficial—most of that money is to complete the funding for this fiscal year that we are currently in. The continuing resolution expires March 6, 2009, and I know that because GAO is one of the entities under the continuing resolution. But I would say—and this relates to the Recovery Act as well as the omnibus—that I think there ought to be some flexibility to maybe shift some of the time frames for when the money is spent to allow for the type of examination that you are talking about, even if we are talking about some of the balancing between spending quickly and spending wisely. And I think there are some provisions in the bill that if States do not spend money, certain money like in the transportation area, within 120 days, that money gets reallocated to other States.

So I think this is something that needs to be monitored carefully, and there ought to be some flexibility built in to make sure that when those two choices are there, “wisely” is equal weight to “quickly.”

Senator COLLINS. Thank you. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks, Senator Collins.

We will now go to Members of the Committee. I appreciate the attendance. We do so, as is our custom, in order of appearance. For the information of the Members, the list I have is Senators Burris, Voinovich, Tester, McCain, and McCaskill.

Senator Burris.

#### **OPENING STATEMENT OF SENATOR BURRIS**

Senator BURRIS. Thank you, Mr. Chairman, and I would like to thank the panel.

Because, as you know, I am an old State auditor, State comptroller, and a member of the National Association of State Auditors, Comptrollers, and Treasurers (NASACT). I am glad to see that you are involving the NASACT in that, Mr. Dodaro. That is a great organization for dealing with what we can do on the State level.

But, every day I receive calls in my office from constituents wanting more information on the Recovery Act and how those dollars are going to be spent. And after reading your testimony last night, I have a better idea how it will be disbursed and also great confidence in the transparency, accountability, and the oversight provisions. OMB, GAO, and the IGs, such as Ms. Fong, you set the bar very high. I just hope and pray that we will be able to execute on that bar that we have set.

I wonder if you, Mr. Nabors, could just give me a walk-through example. If you send to our Department of Transportation (DOT) in the State of Illinois, let us say, \$2 billion for construction or for highway programs, I know how the money flows in the regular program. What is different now with the Recovery Act funds that are going to come in as opposed to the other funds that will be coming in for our highway construction, for example?

Mr. NABORS. Well, I will answer that in two ways. In one way, there is not a lot that is different. It is coming through the same programs to the same people. In a separate way, though, there has been a higher level of scrutiny that has been placed on Recovery Act funds than had been placed on normally appropriated funds. Within the Executive Branch, we have created separate Treasury accounts for Recovery Act money to better allow us to track how that specific amount of money is being followed. And I think that in terms of the types of conversations that you will hear from the President and from other members of the Administration, I think that you should expect to hear a greater desire about how those funds are going to be spent.

Normally, the transportation money, for example, goes to the States, and the States have a great deal of flexibility as to how they spend that money. I think that you will hear the Administration talking about not just getting the money out but recommendations and suggestions on how that money can be most effectively spent.

Senator BURRIS. Now, will there be some type of extra sign-off on these particular funds in any way? Or would that procedure still be the same?

Mr. NABORS. There are special reporting procedures and certification procedures that are set out in the Act, which we are working with the governors and the State and local officials to clarify. But, yes, there are special sign-off procedures related to making that money available.

Senator BURRIS. Perhaps Ms. Fong or Mr. Dodaro can answer this question, but will we be able to track that once those sign-offs are done? Will there be any up-front assessments in the State agencies or the cities or the municipalities where these funds will end up? Let us say it is a water project that is under the Recovery Act. Will there be any advance looking at that project by any of our governmental agencies, or will that all be certified by the local, State, or municipality that received those funds?

Mr. DODARO. For the States and localities that we will be visiting, Senator Burris, we will be looking at that process that they use to make those decisions. Now, it would be inappropriate for us to insert ourselves as independent auditors before the management makes the decisions. But once those decisions are made that will

be something that we will be reviewing. We will also be talking to the State auditors and the local auditors about their work with regard to those issues. But that will be our goal in tracking the uses of the funds going forward.

Senator BURRIS. I am trying to get at the fraud or abuse of the funds, whether or not that project really was a worthy recovery type of project. And in hindsight, let us say we spent \$15 million on that sewer treatment plant and it was really determined that this was something that was probably not needed by the municipality, will we run into something like that, or is that what you will give some type of report on after it is done?

Mr. DODARO. Well, we will try to track that real-time as those decisions are made. I think the other really unique feature of this whole thing is that from my understanding, once these projects are awarded, they are to be posted on Web sites by the States and localities so that they would be visible to a lot of people. We can look at the justifications that are there. I think it is a potentially very good development that this level of transparency will be there, and I think that is a unique aspect of this.

On some of these issues, you will be able to perhaps look at the justification and raise some questions. On the other hand, it may be a management prerogative or a decision for which discretion is given to the State and local officials, and we will have to take all those things into account.

Senator BURRIS. Perhaps this is the most important question in this hearing today. How can the Committee and the Congress as a whole aid in your efforts to implement the Recovery Act? The onus is on all of us to work together and get this done right. So what can we do to make sure that you all were able to implement it? Mr. Nabors, I think that would fall in your bailiwick, right?

Mr. NABORS. Well, I think that the most important thing that Congress can do is hold these types of hearings, hold us accountable, make us bring the facts to light so that you have the opportunity to do what Congress does, which is to both legislate and provide oversight of Executive Branch activities.

I think that we will be most successful when all of the information about what we are doing is public, and only when we do that will the public regain confidence in its government.

Mr. DODARO. I would just add to that, that I agree the oversight by the Congress is pivotal here, I would encourage the Congress to conduct oversight of the individual departments and agencies and really let the departments and agencies know that the Congress is very interested and concerned about what they are doing.

Senator BURRIS. Because we cannot make any mistakes here. This is our last shot at the public coming down on us.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator Burris. Senator Voinovich.

#### **OPENING STATEMENT OF SENATOR VOINOVICH**

Senator VOINOVICH. Thank you, Mr. Chairman.

I have never seen such anxiety in this country as I do today. We need to restore people's faith in the future, restore our credit markets, restore our housing values, deal with the human needs that



are there that we are experiencing and will be experiencing, and last but not least, create jobs. We are looking for something to happen relatively fast to kind of turn this thing around so people are starting to say we have a future, start spending some money, and we are moving in the other direction.

We have a human capital crisis—Mr. Dodaro, in many of the agencies. I am really pleased to hear what you are doing. You have some flexibilities, I think, to hire back annuitants in your department. Ms. Fong, does the inspector general have similar authority?

Ms. FONG. We cannot do it directly. We need to get waivers of the dual compensation provisions from the Office of Personnel Management (OPM).

Senator VOINOVICH. Go back to OPM and get it.

Ms. FONG. Exactly.

Senator VOINOVICH. Mr. Nabors, you are talking about your great people back in your shop. How many people are you going to have to hire so you can do the job that you traditionally do at OMB and take care of all these things that you just talked to us about? I am concerned about that. I am also concerned about the use of the flexibilities. If you have looked, Mr. Nabors—and I suspect that you have—at what agencies are going to need additional people? What kinds of people are they going to need? Do we have the flexibilities to bring these people on in a timely manner?

It is the human capital part of this, I think, that is really important.

Second is how fast you get the money out on the street, and you mentioned the States are involved. I think you will find around the country that you have State legislators that are involved right now deciding who is going to get the money and how is it going to be put out on the street. And I think unless you, on the national level, through OMB, or through other agencies, basically say to folks, look, get it on the street—and they have 18 months. But we really need to move very quickly to get the job done.

I would like all of your comments about where are we with human capital. Do we have the flexibilities? What are we doing to reach out to the States? Mr. Dodaro, you said you are going to 16 States. What are they doing to get the money out on the street? How do you push the governors? How do you get a letter to the legislators saying, hey, we gave you a bunch of money and we expect you to start to move it.

I would like your comments about those two areas.

Mr. DODARO. I will go first. On the human capital crisis situation, I think you are exactly right, Senator Voinovich. My suggestion would be—and the OMB guidance talks about the flexibilities for the acquisition workforce—that they do have the ability to bring back retired annuitants and experienced people. So I would hope that the agencies exercise that flexibility.

However, I do believe that in this type of emergency situation, OPM ought to consider some blanket authority or waiver to allow more flexibility to—

Senator VOINOVICH. Mr. Nabors, have you talked to OPM about that? Have you done an inventory of all the departments and what they are going to need?

Mr. NABORS. We have started our conversation with OPM, and we are looking at the authority that currently exists, things like rehiring annuitants, using direct hire authority, and veteran's preference. What we are trying to do is to come up with the universe of authorities that exist right now, see how successful we can be using those authorities, and then go from there to what additional authorities might be necessary.

Mr. DODARO. Because this is one area that I had suggested back in the Year 2000 (Y2K) computing crisis, and they gave a blanket authority because a lot of the COBOL planners had retired that wrote the original code and they brought them back. So I think this is very effective.

If each agency has to go individually to OPM to get the authority, it is going to take too long for this period of time. So I am encouraged to hear that they are outreaching. So I would say that would be issue No. 1, because those people can come back right away. They are not concerned about the time frames here. It fits within the ability to be able to do that. So I would say that is very important.

We will be working with the States. We expect to be in the States this month. We will be talking to them about their processes.

Senator VOINOVICH. Mr. Nabors, are you aware of what is going on out there?

Mr. NABORS. In the States?

Senator VOINOVICH. Yes.

Mr. NABORS. Yes, I get calls from mayors and governors just about every day.

Senator VOINOVICH. It is just the whole issue of prioritization. In Ohio, we have \$2.7 billion worth of highway projects that are shovel-ready, but we only have \$1 billion available in stimulus funds. The question is which billion do you select. Or sewer and water, Ohio will receive \$247 million, but we have a \$6 billion need. By the time they figure it out, it could be too late.

Mr. NABORS. While trying to be respectful of State and local processes as they make decisions about which projects need to go forward, we are emphasizing in all of our conversations that the money does need to be spent. In certain instances, Congress has actually written in requirements that if you do not spend the money, Congress will take it back and reallocate it.

That has both a plus and a minus. One of the fears that I have is that incentives like that may lead to some questionable projects being funded simply to make sure that the money does not go back. But we will continue to work through the processes with the flexibilities that we have.

Senator VOINOVICH. If it was not for the money they got there, a lot of them would be in terrible shape. So I think we have a little hammer on them.

We have all kinds of reports. We have reports that OMB is going to, every 2 weeks, ask people for reports, or every week? Then you have the inspector general. Then you have Mr. Dodaro doing his thing. This group, that group, and everything else. [Laughter.]

I am just wondering, is everybody going to be doing the reports? Who is going to be doing the work?

Mr. DODARO. Right. Well, I can speak at this from a couple different perspectives. First, like the TARP program, where we have to report every 60 days, we have these bi-monthly reviews. We will be able to meet our requirements. We will be doing the audit work. We will be out in the field. The unique perspective that we will bring is looking at the State and local sector across all the Federal programs and the flow of funds. So our reporting under this particular act will be unique in that respect, and we will have people out doing all the audit work. I am not concerned about that, Senator, really.

Senator VOINOVICH. Mr. Nabors, you ought to do an inventory of how many reports everybody is going to have to do.

Mr. NABORS. A lot.

Senator VOINOVICH. And find out, does this make sense, because particularly in the first 6 months with people getting started, finding out how to do things, and then they are filling out all these reports. Do they want us to do this or are they more interested in the reports?

Mr. NABORS. Well, I think what I would offer at this moment in time is that what we are doing is unprecedented, and I think we appreciate the amount of attention that people are paying to oversight at this moment in time. We will get better at this as we go through, and we will come up with streamlined procedures, best practices that our first weekly reports were due this week. I think we have 23 out of the 25 agencies that have reported, which is fantastic. As we get better at these reports, hopefully it will be less of a burden on the agencies.

Ms. FONG. May I offer a comment on the reporting? Just from the IG perspective, we are looking to not spend a lot of time putting together our formal, traditional audit reports, but to actually get in there and give agencies our advice and our recommendations in as quick a fashion as possible. So you will see fewer traditional IG reports, but hopefully you will see more advice and helpful recommendations coming out.

Senator VOINOVICH. Great.

Chairman LIEBERMAN. Thanks, Senator Voinovich. And you are right. We reacted in this emergency with an unprecedented spending program and a pressure to spend it quickly. But we are all concerned, as the public is, that there is a risk it can be spent inefficiently and even fraudulently. So we create these layers of oversight, but then we have to make sure that the layers are well and efficiently implemented. That is part of what we want to do by regular public hearings, and I know it is what the three of you want to do as well. Thank you.

Senator Tester.

#### **OPENING STATEMENT OF SENATOR TESTER**

Senator TESTER. Thank you, Mr. Chairman. I want to thank the folks for testifying today.

I think each of you, maybe with the exception of Mr. Nabors, talked about reaching full staffing and hiring a bunch of people. When do you think full staffing will be achieved, Ms. Fong?

Ms. FONG. Well, we are aiming to have most of our staff on board by the end of the fiscal year, and that is reality. Now, we will be

looking to try and get some waivers through OPM on the re-employed annuitant issue, and that will allow us to bring people on much faster. So if we can get that done, we will be able to do it sooner.

Senator TESTER. Mr. Dodaro.

Mr. DODARO. By the end of the fiscal year.

Senator TESTER. Are you doing any oversight right now? I mean, the money is just starting to flow out at this point in time, which is commendable. I commend the President for that. Is there any oversight going on right now of expenditures?

Mr. DODARO. Well, since our focus is on the State and local level, we will be in the States. We have not been to the States yet, or localities. We will be there this month. We needed to wait until they received the money and made some decisions on how they were going to use it. We did not want to show up prematurely.

Senator TESTER. No.

Mr. DODARO. For reasons that we talked about.

Senator TESTER. Right.

Mr. DODARO. But we are going to be there this month, and our first report is due next month.

Senator TESTER. Ms. Fong.

Ms. FONG. Yes, I can speak from my experience at USDA. We are actually issuing audit reports this month on a couple of programs that are receiving stimulus funding, in particular, the broadband program. And there will be some very specific recommendations to those managers.

Senator TESTER. Along those lines, as things unfold here, how much are you depending on the States for their oversight functions?

Mr. DODARO. Well, as I mentioned, I have talked to State auditors and local auditors, so what we are going to do is see what they are doing.

Senator TESTER. OK.

Mr. DODARO. And we will rely on that, first for the coordination issue, not just at the Federal level. It is also at the State and local levels.

Senator TESTER. Absolutely.

Mr. DODARO. And I am committed to build on what they have done.

Senator TESTER. So in a time of tough budgets, as Senator Voinovich talked about, I can tell you that one of the things that States will probably be cutting out is staffing, and some of that staffing may be in the area of oversight. How are you going to deal with it? We are talking about 16 months, assuming 80 percent of this money goes out—which, by the way, I applaud that for good projects. How are you going to know if the States are doing their job?

Mr. DODARO. Well, from our standpoint, we are going to get out in the field. I have senior GAO leadership for each State. We are going to have a team. We are going to be there. That is why I wanted to stay with the 16 States for a period of time, Senator, so we could figure it out. If you are popping in and out, you are not going to be able to do it.

Senator TESTER. OK.

Ms. FONG. With respect to USDA, we have the Food Stamp Program, which receives massive amounts of money, and it transfers it right down to the States.

Senator TESTER. That is correct.

Ms. FONG. And then it gets put out to individuals. We have always worked very closely with the State governments to oversee that program to make sure that eligible people get money, ineligible people do not get it. We are ramping up our efforts to intensify our collaboration with the State and local officials, and we will do more with them.

Senator TESTER. All right. There are some great measures taken in this whole thing, and I commend you all in the work you are doing, and I will get to that in a minute. But one of the things that I think occurs to everybody in this position as we put that bill through to stimulate the economy, create jobs, and build infrastructure is what happens to the people who get money and do not spend it correctly and you are paying for a backhoe that is idling in somebody's yard instead of digging a trench to put in a water line? You have allocated the money. The money has been spent. The contractor has it. They did not do the job as planned. You guys know it. What do you do?

Mr. DODARO. Well, the first thing you do is report it and make sure that it is visible. And depending upon the nature of the offense there are potential remedies. But I think transparency is the real key here, to raise it up to the proper authorities to—

Senator TESTER. I agree. What are the remedies?

Mr. DODARO. Well, you have clear remedies if there is—

Senator TESTER. What is the range of remedy?

Mr. DODARO. Well, there is a range—from fraud, if there is fraud, there is a normal process for those type of penalties. The other types of penalties would have to flow from whatever the State or local response would be in this particular case, or the Federal level recourse for getting reimbursement. It depends on the grant provisions and the contract provisions. That is why it is important to have those spelled out so you can take action.

Senator TESTER. All right. You have talked about guidance; you have talked about making the controls evident; you have talked about transparency and accountability. All that is good stuff, by the way. It is all really good stuff. I assume each one of you have probably been with your individual department for a number of years. You just did not come in the first of the year. You have probably been there awhile?

Mr. NABORS. I have been at OMB since January 20.

Senator TESTER. OK. So I was wrong. [Laughter.]

Mr. DODARO. I have been at GAO for 36 years.

Senator TESTER. OK. Well, you make up—

Mr. DODARO. I am settling in.

Mr. NABORS. We average together 18 years.

Senator TESTER. Yes, 18 years apiece.

Ms. FONG. And I am in the middle. I have been at USDA 6 years.

Senator TESTER. Well, these things that you are doing, it is great stuff. Especially when you talk about what happened with Hurricane Katrina, and what has happened in Iraq with some of the spending there. Why isn't this just standard operating procedure?

And do you anticipate it being standard operating procedure from this time forward? Or do you think at the end of this 24-month period that you are going to be cutting a bunch of people loose and you are going to go back to the way things used to be? Oversight of money is critically important. People are always talking about government waste, and there is waste in the private sector, too. But government waste is tax dollars. Do you anticipate your jobs changing going into the future because of this?

Mr. NABORS. From OMB's perspective, I think that before Recovery.gov was stood up, we had USAspending.gov, and I know that there has been some frustration as to the financial reporting that has been put on there. I think that we are using Recovery.gov to test-drive a number of different concepts that we have, and I think just in that one narrow area, if we are successful in terms of making money transparent, that type of thing will filter over into other activities.

Senator TESTER. So you do not see it as much as manpower, more transparency?

Mr. NABORS. I think manpower will be important, but transparency is going to be important as well.

Senator TESTER. Mr. Dodaro.

Mr. DODARO. I am hopeful that the attention being given to this issue right now will transform itself into more fundamental changes and better management. You need more people to manage these contracts and grants if you are going to eliminate waste. We face an ominous Federal budget situation going forward. It is not just this situation.

Senator TESTER. I hear you.

Mr. DODARO. We have a long road to travel together in this area, and better management is essential.

Senator TESTER. Ms. Fong.

Ms. FONG. I would say that the techniques and the work that we are bringing to bear on this issue are not drastically different from what we normally do in our oversight of agency programs. But what has changed is the intensity and the time critical of the issue. And I think that urgency is what really makes this unique.

Senator TESTER. Well, I thank you very much for testifying today. Thank you very much.

Chairman LIEBERMAN. Thanks, Senator Tester. Excellent questions. Senator McCaskill.

#### **OPENING STATEMENT OF SENATOR MCCASKILL**

Senator MCCASKILL. Thank you. I do not know where to start.

Let me start with the Single Audits. It seems to me that we ought to figure out a way to wipe out A-133 Compliance Supplements for the next 2 years and require every Single Audit to be completely about this money, and I wanted to get your response to that idea. For the record, the Single Audit is a required audit that States must do for Federal money.

Now, knowing the folks that do Single Audits, they get tired of looking at the same programs every year. I think the auditing community at the State level would be thrilled to accept this challenge, because—and it would be just for the 2 or 3 years that we are tracking this money. Frankly, most of the oversight and controls

are in place for most of the Federal programs they audit every year. They may find a little bit of problem with a reconciliation, or maybe they may find a problem in the child support program or some of the other Federal programs. But this is a huge enchilada that has been put on their plate, and it seems to me we could unleash all of those State auditors that know about how to audit Federal money to do nothing but these funds on an emergency basis for the next 2 or 3 years.

Now, first of all, what do you think of the idea? And, second of all, what would it take for us to legally require that?

Mr. DODARO. First of all, I think it is an excellent idea. If something does not change with the Single Audit procedures, it is too little too late going forward. And bringing the State audit community in earlier, the local audit community—I had mentioned in my opening statement I have already outreached to them, to try to engage them to help GAO coordinate with what we are going to do.

I think you could implement what you suggested. But I do not know if OMB has the authority to do that administratively. They can change the A-133 Compliance Supplement. You are talking about a radical change, which I would endorse. I think it is a really good idea. The only amendment I would make is to require internal control testing now and not wait until the end of the year with the Single Audit.

But I think they have the capabilities. They have already asked and talked to me about funding. They will need some support. But the normal support that they receive, I think, should be sufficient if you change the requirements.

Senator MCCASKILL. Yes. I mean, you would not need any additional personnel—they have the staff in place. In fact, we are beginning the Single Audit season as we speak.

Mr. DODARO. Right.

Senator MCCASKILL. The teams in every State are right now looking at A-133, figuring out which programs they need to look at. They are doing their scopes. They are doing their plans. And why could we not just say we are going to tell you to forget about A-133, we want you this year in the Single Audit to look at the controls that are in place for this money that is coming, and next year in the Single Audit we want you to evaluate those controls and how they are working. It would be a perfect way, without spending any extra money, for us to look at an unprecedented amount of money that is flowing quickly into the States. And if we had to amend a law to do that, I think we could probably get that done. I think we could probably get both sides of the aisle to agree to something like this that we could quickly do. And I think that the State audit community would embrace it because they would like to be challenged in this regard. At least I know the line auditors would, because they are sick of doing the same old Single Audit every year that nobody pays any attention to. They would like to do a Single Audit that somebody reads.

Mr. DODARO. I think it is a great idea.

Ms. FONG. I think from our perspective it is a great idea, and I would love to have some time to think about it and give you some comments on that.

Senator McCASKILL. Well, if you guys would, and I would particularly like, Mr. Nabors, for you and the team at OMB to think about that. I know if we try to change A-133, trust me, I know it will not get changed until 7 years from now. I mean, the notion that we could do this by making announcements about A-133, that we are going to change it, and then taking comments, and then somebody is going to write it awhile, and then somebody is going to look at it awhile, and before you know it, we will change A-133 to audit these recovery funds, right about the time they are all gone. So it would take the government doing something we do not do very well.

Now, we just did something pretty bold. It seems to me that we could be just as bold with oversight as we have been with spending the public's money. And it seems to me they need to go together. So I would hope that the Administration would take a serious look at this, and if you all could maybe—Mr. Dodaro, if you would reach out to the State auditing community and get their response, I would be shocked if it was not positive.

Mr. DODARO. I would too. But I will do that.

Senator McCASKILL. All right. Let us see if we cannot get that done.

Mr. DODARO. OK.

Senator McCASKILL. The second thing is I am a little confused about the Web site. I do not believe the Web site belongs with the Recovery Board. I think that is a huge job for a temporary group of folks. I think it belongs at OMB. That is where the data is. I had an amendment to do that, and we did not get it done. But I think OMB needs to really stay hooked up on this Web site because it is unrealistic that this board is going to be able to do what we have advertised that this Web site is supposed to do. And, specifically, I want to talk about the detailed guidance you guys gave to reporting requirements.

On page 14 and 15 of the OMB's guidance document for the Recovery Act, dated February 18, 2009, I am a little confused because it seems to indicate that the only recipients that need to report is, in fact, the prime recipient. What it says is "prime recipients." Now, obviously the agencies have to report, but I am talking about the money that is going to the State.

What the guidance says, which is very troubling, is if the State A gives the money to City B, who hires a contractor to build a bridge, and then hired a subcontractor to supply the concrete, OMB is telling the State that all State A has to do is report the subgrant to City B. But City B has no requirement to report anything.

Mr. NABORS. Right.

Senator McCASKILL. So how do we get to the contracts?

Mr. NABORS. Well, I think that in putting out the guidance, one of our chief concerns was reporting burden with regard to small businesses. We have a strong desire to get to the very last contract, if at all possible. But one of the things in the quick timetable that we were looking at, both with the legislation and putting the guidance out, was that we could not have a system or a structure in place that would sufficiently reduce the burden on small business or perhaps individual contractors in such a way that it would not be overly burdensome.



As we are going through the guidance process, this is the type of thing that we will be looking at, though. This will always be a tension. How far can we drill down into the data? And I think our commitment is to drill down just as far as we can possibly get.

Mr. DODARO. I would just add, this sub-recipient issue has been a nettlesome one for a long time. I think this would be a good pilot exercise, before the money disappears. You could set some thresholds on this so you are not reporting things below a certain level.

Senator McCASKILL. Well, the law has a \$500,000 threshold.

Mr. DODARO. Right. You need to have this information if you are going to properly track this.

Senator McCASKILL. I have to tell you the truth. If a city in my State gets \$5 million to build a bridge, and that is all we know, I tell you, that city is going to be bothered because my staff is going to be calling them and wanting to know—they are not even required to say whether they competitively bid it.

I just think this guidance does not match what we have advertised. And I get the reporting requirements are tough, and maybe there are ways that we can streamline that. But if we are actually saying that all the money going to the State, all the State has to do is say what city got it or what program got it and that is it, I do not think we get to competitiveness; I do not think we get to the issues that many of us have staked our reputation on that we are going to try to do this. And to start at the very beginning and say you do not even have to report who got the money in terms of the contract, I think that is problematic.

So I would ask you guys to take a look at that. I know this is not final guidance. I know this all came really quickly. But I would ask you to take a look at that, and I will save my other stuff for the next round. Thank you.

Chairman LIEBERMAN. Thanks, Senator McCaskill. I was just thinking that in the U.S. Marine Corps they say once you are a marine, there are no ex-marines. So I think in your case, once you are an auditor, there are no ex-auditors. [Laughter.]

Thanks very much. You really make a contribution to the Committee. We will do a second round as long as Members want to have another 7-minute round.

Incidentally, I will say with regard to one of the questions you asked, at a staff level there were some very preliminary discussions with Mr. Devaney, and I think it is fair to say that he understands that the law says that the board has the primary responsibility for the Recovery.gov Web site, and a lot of their money will be used to staff that up. But OMB has started it, and I think he envisions a cooperative relationship between the two. But I am sure you all will work that out as it goes on.

Let me focus in on this question of fraud. I mentioned earlier that the Department of Homeland Security (DHS) Computer Emergency Readiness Team had found out about scammers offering economic stimulus payments fraudulently in an attempt to steal personal data information from those who respond. Human nature unfortunately tells us when you have this much money out there, quickly being spent, in one or another way people are going to try to take advantage of it and rip off the money.

What are the standard moves that you make as inspectors general at GAO, to try to ferret that out? Because this is going to be a lot of money going out to a lot of people pretty quickly. And obviously we have the whistleblower protections here, so you hope that will help with people involved directly in the public and private sector. But do you do random checks? Do you use undercover people? How are we going to work to prevent fraud in the use of this money?

Ms. FONG. Let me take a first crack at that.

Chairman LIEBERMAN. Go ahead.

Ms. FONG. We are aware of a similar situation that occurred in one of the departments—I think it was the Small Business Administration (SBA), actually—where there was someone in the public who was attempting to hold themselves out as an SBA official, and they were trying to get personally identifiable information (PII). The IG became aware of it and worked with the administrator of the agency. They squashed the fraudulent bulletin. They went out and issued releases to the public, and also to their recipients of funds, saying, “If you are contacted by anybody holding themselves out to be a Federal official saying ‘Send in your PII information,’ do not do it.” They have also issued some public information notices, and most importantly, they have notified all the rest of the IG community that these scams are going on.

And so what we are doing in our own departments is going out to our officials and saying, “Hey, this went on at SBA, it could happen with us, we need all of you to be aware of these potential scams, please let us know when you see them, and then we will pursue it through all of our prosecutorial means.”

Chairman LIEBERMAN. Well, that is good. And, of course, we hope even by mentioning it here today that people will be on notice. But go beyond that. I just happened to mention that because I heard about it.

One of the worries that I have with all the money going out so quickly is—and this is a subtle kind of fraud, but it is a fraud—that we will end up being overcharged by various contractors who will be getting stimulus funding. We should not allow ourselves to be overcharged.

Mr. DODARO. Yes, there are at least two issues in addition to the awareness feature that Ms. Fong talks about, which is very important. One is to look at the design of the controls for the program up front or the testing of the eligibility requirements. Are they verifying with other data sources up front?

But we also plan to do proactive testing whereby we would use undercover identities. We would test the system. The \$1 billion that Senator Collins mentioned in the FEMA program and Hurricane Katrina was a result of our people doing a statistical sample and then projecting from that using identities to test the system to make sure that people who are not eligible were not receiving benefits—or even testing whether or not you can receive a provider status under the Medicaid program and not have a real entity.

So we plan to do targeted testing up front to try to test these systems, but you also look at the design and the controls.

Chairman LIEBERMAN. Ms. Fong, do you want to add anything? I know you spoke first about the kind of consumer scam, but from

the IG perspective, what else can we expect the IGs to do to try to ferret out fraud here?

Ms. FONG. Well, one of the things that we are doing at USDA is building up our data capacity, and what I mean by that is we are starting to go to the agencies and looking at the data coming in on program monies and participants to identify anomalies in that data, which is sort of an early-warning system for us.

When we identify situations like that, we can then go out—

Chairman LIEBERMAN. Excuse me. What kind of anomalies, for instance?

Ms. FONG. Well, for example, if benefits are being passed out through one of our programs—and we notice in some of the data fields that there are a number of indicators that perhaps some people should not be getting these benefits, for whatever reason. It depends on the eligibility criteria.

Chairman LIEBERMAN. Right.

Ms. FONG. Then we would be able to take that data, go out and do some testing, do some undercover work if we need to do that, which is a traditional tool that we use quite a bit at USDA, and start working with the program managers to say, “Hey, you need to be looking out for these red flags, go after these red flags, and we will pursue individual cases as well.”

Chairman LIEBERMAN. I am really glad to hear you are using undercover agents, and I want people to know that you are using undercover agents because this could be different to those who may be hatching plots to defraud the public of some of this money.

Mr. Dodaro, I was very encouraged by some of the proactive steps you are taking with regard to the tax cuts in this program, and they are very important. So I gather part of the aim here is not only to make sure that people get the tax cuts, but to put you in a position to evaluate the impact of the tax cuts. Is that right?

Mr. DODARO. Yes, that is correct.

Chairman LIEBERMAN. Why don't you talk a little bit about what you are looking for in the evaluation?

Mr. DODARO. Oh, sure. These would be not in the amounts of money being reduced, withholding, or the amount of checks that are sent out to people. This is for the tax provisions.

For example, there are provisions in there that allow Recovery Act bonds to be provided. But unless IRS identifies who is giving those bonds, a lot of this gets rolled up in part of the tax reporting of the entities, and you cannot determine at the end of the day how many of those bonds are issued or whether people are getting credit for creating certain jobs and taking that credit. But if it is rolled up with other information IRS collects and not separately identified by IRS, that will not happen. The same for depreciation. There are some depreciations that are allowed under the Act.

Those are just three examples. There are many others that are in there, and our experience has been over the years that when Congress turns to us a year or two down the road and asks us to evaluate the effectiveness of some of these credits—the Enterprise Zone credit is one that we were asked—you cannot do it.

So what we have been trying to do is proactively identify these areas so that IRS can track it. This is equivalent to Senator McCaskill's question on the sub-recipient level because IRS is con-

cerned about the burden on the taxpayers, but the real issue is if Congress really wants to know whether or not the amount of money that has been foregone, if you will, or provided through tax relief here—which is significant, it is over \$200 billion—is actually producing what the Congress intended, you need the data to be able to do it.

In any one year, tax expenditures can be more money than total discretionary spending. And we have advocated for a while now that more transparency, visibility, and re-evaluation of those tax provisions be a normal part of oversight in the Federal Government.

Chairman LIEBERMAN. That is very important. I appreciate it, because obviously—and, of course, we will see some of this from the macro economic data, but we hope that the tax cuts will encourage people to spend, because consumption has been falling so fast and not driving our economy in the way it normally does. Thank you very much.

Mr. DODARO. You can also have tax fraud in some of these areas, and that is something else we will be taking a look at as well.

Chairman LIEBERMAN. What are you thinking about?

Mr. DODARO. Well, this would be in some of the administrative areas and whether or not some of the payments were made; people are claiming credits that may not actually have the justification for.

Chairman LIEBERMAN. Thank you. Senator Collins.

Senator COLLINS. Thank you.

Mr. Nabors, I want to associate myself with the questions that my colleague from Missouri asked you about the guidance that is being given. The intent—indeed, the letter of the stimulus act—requires Federal, State, and local governments, but also private businesses, that are receiving money under the Recovery Act to adhere to the transparency and accountability requirements. The initial implementing guidance that OMB issued on February 18, seems to indicate that you are looking at tracking only at the macro level.

For example, the guidance states that sub-grantees, including contractors and subcontractors, do not have any specific reporting requirements for the purposes of reporting to the Recovery.gov Web site.

I just want to alert you that that concerns me, because if we are truly going to follow the money, which is the goal, we have to be able to track it down to the level of those who are the actual recipients, not just those who are passing the funding on.

And so I hope that you will take a look at this issue as you issue more detailed guidance. I am not trying to burden small businesses with unreasonable reporting requirements, but we do have an obligation, if we are going to be tracking the money, to look at where the money goes.

I think that Senator McCaskill has raised an important point, and it is a point that I had intended to raise as well.

Mr. NABORS. The points that you have raised are very important, and we will take that back.

Senator COLLINS. Thank you. Mr. Nabors, you may be aware that the 2009 Defense Authorization Act, as a result of provisions that Senator Lieberman and I authored, required the establish-

ment of a government-wide Contingency Contracting Corps. Our vision in authorizing such a core of experienced contracting officials applies exactly to this kind of situation where there is a need to have money allocated and under contract quickly, but we need experienced personnel to ensure that it is also done effectively and without shortchanging the need for competitive contracting.

The Corps would be a very useful asset to have in place for the stimulus funding. Could you tell me the status, if you are aware of it, of establishing this Corps and where this falls on the list of priorities that you have?

Mr. NABORS. Well, I am aware of the Corps. We have had some initial conversations, not just with regard to the Recovery Act, but in terms of the President's commitment to essentially clean up the way Federal contracting is done. And we have evaluated, or we are continuing to look at this as an important tool.

I cannot give you a specific timeline or prognosis as to when you would see the Administration come forward with a specific proposal to implement this, but I can tell you that it is very much on people's radars right now.

Senator COLLINS. Ms. Fong, you mentioned the number of additional auditors and investigators and human resources individuals that you are looking to hire, and, of course, that is being repeated across the Federal Government. I am not concerned about your ability to get the human resources people, but I am very concerned about whether or not GAO and the IGs, in particular, are going to be able to find the number of auditors that are going to be required.

We have seen with the Special Inspector General for Afghanistan a terrible time in his efforts to staff up his office. Now, granted, it is a lot harder when you know that you might be deployed to Afghanistan than to cities around the United States to audit the stimulus spending. Nevertheless, I am concerned about this.

I am also concerned that the Federal hiring process is so encumbered with regulation that it is very difficult to hire people quickly, even if they are superbly qualified.

Do you have any recommendations to this Committee for helping you cut through the bureaucracy for hiring the people that you need?

Ms. FONG. Well, you are exactly right. This is one of the major challenges we are facing.

I think in our view—and I have talked to a number of my colleagues in the community—if we can bring on board people who have left our offices and retired, if we can re-employ them as annuitants, that would do a lot to solve our problems, because they are properly trained, they know the programs very well. They can just get on board and start running right away.

Now, the trick on that, of course, is that under the current legal structure, we have to go to OPM, and we have talked today about the need to work with OPM very closely on that.

Obviously, one of the issues that we could put on the table is if there is any legislation working its way through Congress right now on re-employed annuitant authority, perhaps consideration could be given to us. That would be a wonderful thing.

Senator COLLINS. Ms. Fong, there is a huge disincentive for annuitants to come back, as their pensions are offset by their salaries. And Senator Kohl and I have a bill that would solve that problem. I would ask you all to take a look at it, because I think if you are looking at re-employing annuitants, we have to take away the huge financial disincentive for them to come back to work.

Mr. DODARO. Senator Collins, we at the GAO have the authority to waive the annuity offset provision. We have our own personnel authorities, and so I have no doubt we will be able to find the right people. But on your point about re-employed annuitants, over the past few years we have hired about 80 people that way, to come in for specific projects for specific periods of time. It is wonderful, and I would endorse whatever you could do to provide legislation to give that authority to others.

It needs to be carefully used, just like any other authority, but in the meantime, there is no reason OPM could not give a blanket waiver for this emergency situation, in my opinion.

Senator COLLINS. I am not sure that OPM has that authority, but we will take a look at that. You have correctly envisioned what my next question was going to be, because I knew GAO did have that authority, and there is a real contrast in your ability to re-employ annuitants who are already trained, looking for a short-term assignment. It is truly perfect for overseeing this money which is going to expire. So I hope, Mr. Chairman, that we can move that bill.

Let me just ask quickly one final question, Mr. Dodaro. It is extraordinarily important that we track the job creation provisions of this bill so that we know whether or not we were successful in creating or saving 3.5 million jobs, which is the estimate for this bill.

Are you working or do you have recommendations for OMB and for us in Congress on how that can be best accomplished? One of the reasons that I am concerned about the tracking is if you do not have tracking going down to the contractor level, I do not know how you are going to be able to estimate with any accuracy at all how many jobs were created.

Mr. DODARO. Yes, we have responsibility under the legislation to look at the recipient reports, specifically as it relates to the portion of the report that they are required to file quarterly on the number of jobs preserved or created.

Now, there are a lot of issues we have been thinking about on this. We have been trying to get up and running on the bi-monthly reviews at the State and local level, and the sub-recipient question was one we had talked about. If that is provided, you will have better data on that. There are definitional issues. What is a job? How do you make sure all the people who are reporting are using the same type of definitions? So we are going to look into that issue going forward.

I think also the recipient reports need to be juxtaposed against macro economic analysis of the job creation. CBO has made some estimates about the number of issues there, and I have talked with the new director, Doug Elmendorf, about trying to use the reviews of the recipient data to test some of the broader trends in the macro economic analysis.

So we are going to turn our attention to the methodological aspects of this soon, and we would be happy to share our thoughts with you.

Senator COLLINS. Thank you. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator Collins. Senator McCaskill.

Senator MCCASKILL. OK, so here is another idea. All the State governments are offering early retirement to experienced auditors because of their budget crunches, and they have made very attractive packages for State auditors to retire. There would be a whole pool of auditors available for this period of time that would not have the annuity considerations. Let me just talk about my love affair with auditors for a second.

These people, you people who do this work, you are not in it for the glory, and you are not in it for the money, because there is very little glory and there is not a whole lot of money. The people who do this kind of work are really public servants. They enjoy the fact that they are doing what needs to be done to look after the way we spend public money. And I think that there is a cadre of these retired people at the State level that would be honored to step up to the plate and help out during this 2-, 3-, 4-year period because of what we are trying to do here. We are trying to save our economy in a way that makes sense for most of America, and I think that there would be a patriotic duty that would kick in.

I can give you five or six names of incredibly good auditors in the State of Missouri that have all retired within the last 2 years, and I think the average amount of time they audited was 25 to 30 years apiece. And they never made six figures. And one of them was in charge of the Single Audit in the State of Missouri for probably 20 years.

Now, here is somebody who understands Federal programs, understands how to track Federal money, and poor Ken Kuster is going to hear about this hearing and go, "I cannot believe Claire is signing me up, and nobody has talked to me."

But I really do think that if you went out to NASACT and said, "Can you give us five to six names in your State of recently retired State auditors that might be willing to come to work for IGs that have all these resources that we hope to get in the bill?" I think you would have an incredibly positive response, especially if you told them they did not have to move to Washington for the rest of their lives, because they are not going to want to come here. They are going to want to stay where they are. But that is the beauty of this, is that you need people out in these States doing this work, and I think that you have a built-in contingency audit force there if you take advantage of it.

This is an awkward thing for me to ask because I think everybody knows how supportive I was of the President during the political season, but I want to talk to you all about the Web site, and this is especially for OMB. This board now is made up of IGs. They are not political. They really do not serve this President. They served the last President and they will serve the President after this President. They are non-political people, for all the right reasons. They should not claim a party. They should not claim an alle-

giance. They should want to just look after public money, period, and we need to protect them politically.

I would like to throw out the notion that we need to be very careful on this Web site to make sure that it is not political. I want to see the President's radio addresses, or hear them every week. But I am not sure that is a link that belongs on Recovery.gov, because he is going to give a lot of radio addresses in the next year that do not have anything directly to do with how we are spending this money.

I think this is a little bit different than the White House Web site or any other government agency Web site where I think there is a natural tendency to promote whatever President is in office. But I think on this Web site, because you have a group of IGs in charge, I just think everyone needs to be very careful that it does not appear to be promoting anything that could even have a whiff of political advocacy. And I would like your take on that, Mr. Nabors.

Mr. NABORS. I concur with your assessment. Part of the reason why we originally envisioned the oversight board taking control of Recovery.gov is to better convey to the public that this is not data that has been cooked through a political process. And I think that OMB will continue to play a role going into the future with the Recovery Board simply because OMB, as sort of the backbone of the Federal Government, has processes in place to actually quickly pull that data in that they are looking for. And I think that we will continue to want to play that type of role.

We are very concerned, though, about the appearance that Recovery.gov may be seen as something other than a fact-based/driven database of information for the public, and I will make sure that your concerns get back to the White House. But it is a sensitivity that has been expressed.

Senator MCCASKILL. Great. And every single picture has our President in it. I think a great photograph that should be on Recovery.gov would maybe be a photograph of the Chairman and Ranking Member of this Committee as it relates to the oversight capacity they have.

Chairman LIEBERMAN. Because we are so non-political. [Laughter.]

Senator MCCASKILL. In this example, you are.

Chairman LIEBERMAN. I appreciate it.

Senator MCCASKILL. For individual reasons for both of you. But this is not about just the President of the United States. This is about having more information about IGs and who they are and what they do, and how they get to the jobs, and more information about GAO. I think people who are coming to this site want to get information about if we are watching their money. I would much prefer links through to a number of reports from GAO than links through to 150 pictures of the President I worked so hard to get into the White House. So, consider that for what it is worth.

Mr. NABORS. I will work to ensure that those links are there in the future.

Senator MCCASKILL. All right. Great.

The last thing I wanted to just mention to you, Mr. Dodaro, was your testimony as it related to contracting. I would welcome any



suggestions you have. I am very excited that the Chairman has created an Ad Hoc Subcommittee on Contracting Oversight. And we have hired a staff director for that subcommittee. She begins on Monday, and we will begin work immediately. I would very much like input on how we can in that oversight committee begin to immediately look at contracts that are being entered into with this money. And I would like us to keep the running tally of competitive versus non-competitive and fixed price versus any other garden variety. And it may be that we can together devise a way that tally is kept, because if everyone knows we are keeping that tally going into it, I think it might have the sanitizing effect that we are looking for. And I would ask that you and also Ms. Fong, in terms of the IG community, to consider that as you begin to get some of these contracts and see them.

I am particularly interested in personal service contracts. I am particularly interested how many people we hire to do services as opposed to building stuff or moving dirt. I think there is a real potential for abuse there.

Mr. DODARO. I would be happy to provide help on that. I think it is a very important issue. It is another good idea. And we would be happy to help.

Senator McCASKILL. Thank you all very much.

Chairman LIEBERMAN. Thank you, Senator McCaskill. I am excited, too, about the subcommittee that you are going to chair, and I think it would be a perfect focus at the outset to take some of the contracts issued pursuant to the stimulus, because, again, we want both the governmental people involved and others to know that we have the GAO, we have the IGs, and we have this Committee overseeing what they are doing.

I want to come back to something Mr. Nabors said. The fact that there have been 150 million hits on the Recovery.gov Web site in less than 2½ weeks since the law was signed by the President is amazing. And I presume, to reach a conclusion that it reflects both the anxiety and urgency with which the American people want to see us doing something to get the economy going again and want to benefit themselves as they understand where the money is going. Also it reflects how much they want us to make sure that the money is spent efficiently and well. And, of course, the law empowers the three of you to play critical roles, and those that work with you, in doing so.

I am very encouraged by what you have said today. I think we are off to a good start. But we have all got a responsibility to stay on top of this because any significant fraud or waste in this program is going to have a devastating blow on public opinion and trust in government.

Our full Committee is going to stay on this, and as frequently as is constructive. I definitely want to come back within the month before we break for the Easter/Passover recess to hear Mr. Devaney and maybe ask you to come back and tell us where you are at that point, and we will continue to do that on a monthly basis as long as it makes sense, to see how much money is out, how is it going, and what are you learning. Maybe there is something that is happening that requires a quick legislative fix, and we can also see what systems you have put in place, Mr. Dodaro, Ms. Fong, and

Mr. Nabors, to make sure that this money is being spent efficiently and honestly.

So I thank you very much. We have a lot of work to do together. We are going to keep the record of this hearing open for 15 days, if you want to add to your testimony, or Members of the Committee want to ask you additional questions. But, most of all, thanks for what you have done so far. We are with you. This is very important to our country.

The hearing is adjourned.

[Whereupon, at 12:05 p.m., the Committee was adjourned.]

## **RECOVERY AND REINVESTMENT SPENDING: IMPLEMENTING A BOLD OVERSIGHT STRATEGY**

**THURSDAY, APRIL 2, 2009**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 10:01 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, McCaskill, Burris, Collins, and Coburn.

### **OPENING STATEMENT OF CHAIRMAN LIEBERMAN**

Chairman LIEBERMAN. Good morning and welcome to this second in what will be a series of hearings our Committee will hold pursuant to our oversight responsibility to monitor how the billions of taxpayer dollars that we have appropriated under the American Recovery and Reinvestment Act, the Stimulus Act, are being spent.

I am going to begin with a quote from Benjamin Franklin, which is always a safe thing to do. "It takes many good deeds to build a good reputation and only one bad one to lose it." And so it is in some ways with the Recovery Act. We all want the Recovery Act to succeed. In fact, we all need it to succeed to protect and create jobs to start our economy growing again. But a mistake, a story about how taxpayer money is being wasted or funneled to improper uses, will really undercut faith in this program and, I suppose, undercut faith once more in government, no matter what other parts of the program are successful.

I understand that is a large undertaking, to say that we will attempt to prevent any misuse of this money, but that has to be our goal because of the importance of this project to our national economic revival. So our Committee wants to use these hearings in cooperation with the Administration, particularly with Mr. Devaney, whom we welcome this morning, as a way together to assure ourselves that we have systems set up to guarantee two things as best we can. One is that the money moves out quickly, which is what we want it to do, but two, that we set up systems that both prevent waste, fraud, and abuse, and also detect potential problems in that regard so we can stop them before they occur.

To help with the very kind of supervision I am talking about the legislation which created the Recovery Act also created a Recovery

Accountability and Transparency Board composed of a chairman and 10 inspectors general from across the Federal Government. That board met for the first time last Friday and its chairman, Mr. Devaney, on loan from his job and good work as an inspector general (IG) at the Interior Department, joins us here today. We look forward to hearing how that first meeting went and what plans or recommendations emerge from that or have been put in place already.

The Recovery Act also included \$250 million for Federal Inspectors General to hire additional experienced auditors and investigators for their agencies and we would like to hear about how that is going.

There is a special problem that we note around the country, and I heard some indication of it in Connecticut, and that is to make sure that State and local agencies, which are now being stretched thin by the recession, in some cases letting people go, have the capacity to effectively manage Recovery Act funds at the State and local level. I am going to be holding a Committee hearing next Tuesday in Connecticut to explore in the State and local setting how the money is being watched as it is being spent at the State and local level.

I am also pleased to welcome again this morning, Robert Nabors, Deputy Director at the Office of Management and Budget (OMB). In addition to providing overall guidance to Federal agencies on Recovery Act implementation, OMB has stood up the Web site, Recovery.gov, which will allow citizens, journalists, and bloggers, to keep an eye on stimulus spending and report waste, fraud, abuse, or theft if they suspect it.

I continue to be impressed by the numbers of usage here. The last I heard, Mr. Nabors—and you can bring us up to date in your testimony—was that the site is getting about 4,000 hits a second. That is astounding. This can be a marvelous tool, not only to monitor Recovery Act spending but to eventually help us develop powerful tools to monitor all Federal spending.

For Recovery.gov to work to its best potential, it is going to need, I think, to allow users as best we can to burrow into the details of where and how the money is being spent. I want to follow up this morning on concerns raised at our last hearing about how we can actually do that, how the data trail can be followed and not turn cold at some of the precise points spending should be monitored, and that is at the specific contract level.

I understand, Mr. Devaney, that the board is taking over responsibility for the content of Recovery.gov while OMB will remain responsible for the collection of data that feeds into the Web site, so I would like to hear from you about how your work is going.

And Mr. Nabors, finally, it is important for us in these regular hearings to get a sense of how much of the money is actually out there. We have seen some glimmering of economic upturn lately. Obviously, employment numbers continue to be bad, but some other indicators have taken an upturn, and I wonder whether some of that may be related to the first spending of the stimulus dollars. Again, we ask these questions in the spirit of trying to make this program work well working together with the Administration.

I close with gratitude to my staff for yet another piece of wisdom from Mr. Franklin. "By failing to prepare, you are preparing to fail." So with our economy at stake, the American Recovery and Reinvestment Act really is too big and too important to fail, and that is what we are all about with your help this morning and every day. Thank you.

Senator Collins.

#### **OPENING STATEMENT OF SENATOR COLLINS**

Senator COLLINS. Thank you, Mr. Chairman. I feel like I should quote Abraham Lincoln or something just to get into the spirit of this day, but I will proceed nonetheless.

Nearly 2 months ago, the President signed into law the American Recovery and Reinvestment Act to help turn around our economy. Now the challenge is to make sure that the billions of dollars provided by that law achieve the purpose of boosting our economy and saving and creating jobs.

As my Senate colleagues and I worked to craft this bill, we established an oversight board and imposed tough reporting requirements to help ensure transparency and accountability in the expenditure of these funds. We remain determined to protect this critical spending from waste, fraud, and mismanagement.

Several provisions included in the law provide safeguards and oversight of stimulus spending. Perhaps, however, the most important is the Recovery Accountability and Transparency Board, created to coordinate Federal oversight efforts. As the Chairman has indicated, the GAO and many of our Nation's inspectors general also have been provided with additional funding to carry out investigations and reporting requirements. A new Web site, Recovery.gov, has been launched to report on expenditures and to provide the public with access to stimulus information. The more eyes that we have on this spending, the better.

The Recovery.gov Web site is now up and running, and as the Chairman has indicated, is tremendously popular. It is my understanding that it has already received some 300 million hits. It is now linked to the individual Recovery Act Web sites for States and Federal agencies. I have included a link to the Recovery.gov Web site from my own Senate Web site, as well as the special Web site I created to provide Mainers with specific information about Recovery Act spending as it relates to our State.

Technology not only allows an abundance of information to be shared quickly with people across this Nation, but also helps to ensure transparency and accountability.

The American people have high expectations for the Recovery Act. The President has estimated that it will save or create approximately 3.5 million jobs and will help to turn the economy around. Taxpayer dollars will be used to improve roads and schools, enhance health care, and invest in infrastructure and science. Regardless of the purpose, each dollar must be spent wisely. Funds need to be disbursed quickly to meet the goals of stimulating the economy, but we must ensure that haste does not make waste or permit fraud and mismanagement. Striking the right balance between speed and caution will be difficult, but it is essential as we administer the grants and contracts funded by this law.

Press reports have already questioned whether some of the first few contracts using stimulus funds were awarded without sufficient transparency and whether contracting mistakes were made. Although the press has generally described these as sloppy paperwork, this is not a reassuring start. Problems like these can easily erode public confidence and leave our economic goals unrealized.

Today's hearing will provide us with a more in-depth look at the most important oversight organization, the Recovery Accountability and Transparency Board. I look forward to hearing from Mr. Devaney, the board's recently-appointed Chairman.

From OMB, I am particularly interested in hearing how it expects to address the challenges of tracking funds at the State and local level, the very issue that the Chairman raised, and ensuring transparency, accountability, and competition in stimulus contracting.

Our government has an obligation to make sure that these vital dollars provide the maximum possible benefit to our economy. The American taxpayers deserve no less from their investment.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you very much, Senator Collins.

We will start with Mr. Nabors. I note, Mr. Nabors, in one of the recent news stories on OMB Director Peter Orszag, it mentioned that he drank a lot of high-caffeine tea during the day. I note the presence of the bottle of Coke Zero there. I share that particular addiction, and with that sense of brotherhood, I now invite your testimony. [Laughter.]

Mr. NABORS. It might be best just to close at that point. [Laughter.]

Chairman LIEBERMAN. Go right ahead.

**TESTIMONY OF HON. ROBERT L. NABORS II,<sup>1</sup> DEPUTY  
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET**

Mr. NABORS. Chairman Lieberman, Ranking Member Collins, and Senator Burris, thank you for inviting me to testify about the implementation of the Recovery Act. Today, I would like to talk about the progress we have made since the last hearing in addressing our shared goal, and that is to implement the Recovery Act as wisely and as quickly as possible.

I will start by talking about where we are with respect to spending Recovery Act funds. As of this morning, Federal agencies have obligated about \$51 billion. That is up from about \$15 billion when we last met. While just two agencies had issued Notices of Obligation at the beginning of March, an additional 13 have done so since then. This includes the Department of Transportation, the Department of Housing and Urban Development, the Department of Labor, the Department of Education, and the Department of Health and Human Services.

In addition to obligations, there is other evidence of accelerating spending activity. Agencies have announced nearly \$151 billion in formula and block grants that will be made available to States. These allocations enable States to foresee important increases to their budgets and can influence States' decision making and benefit

<sup>1</sup> The prepared statement of Mr. Nabors appears in the Appendix on page 230.

the economy even before they are technically obligated. Nearly 500 Recovery Act contracting opportunities and notices have been posted. Seventy-one Recovery Act grant opportunities have been posted. And as of yesterday, Making Work Pay tax cuts were fully implemented, benefiting 95 percent of working families.

Chairman LIEBERMAN. Can I interrupt you on that? I apologize. We will give you more time. But explain what that means, about the Making Work Pay tax cuts. I understood that it might go in, depending on the employers' decision, as early as April.

Mr. NABORS. It actually started in February and there was an April 1 deadline.

Chairman LIEBERMAN. I see.

Mr. NABORS. At that point, it should be fully implemented.

Chairman LIEBERMAN. So the people should really begin to see now, or will see as of April 1, a reduction in the payroll tax.

Mr. NABORS. Exactly.

Chairman LIEBERMAN. I originally had heard that it might not happen until June. Maybe that was during the consideration of the bill. OK, that is great. Thank you.

Mr. NABORS. But it is important to be absolutely clear that while getting funds into the economy is important, it is critical to do so in a responsible and transparent way. This remains a priority for the Administration and the American people who continue to monitor the government actions through Recovery.gov.

As Senator Collins mentioned, the Recovery.gov has had a total of about 300 million hits. That is double the level since the last time we spoke.

Speaking on behalf of OMB, I can tell you that we are taking numerous steps towards effective implementation of the Recovery Act. We are reviewing numerous agency spend plans to ensure that funds are invested appropriately and with sufficient planning ahead of the actual obligations. We have facilitated the launch of recovery Web sites at all major agencies, which are linked through Recovery.gov. We have worked with Federal agencies to improve the timeliness and completeness of their financial reports that are publicly available through Recovery.gov.

And perhaps most importantly, we are preparing to release tomorrow additional guidance to enhance agency reporting requirements and clarify recipient reporting. In order to get the most up-to-date information possible, the updated guidance requires agencies to report more frequently and in more detail. We will ask agencies to provide information about significant funding announcements to OMB as they occur. We are not going to wait. We are going to ask them to report that information to us as the spending decisions occur in order to provide a better real-time sense of what projects are being funded, where they are being funded, and how much funding they are actually receiving.

We will define agency and program plan requirements with a detailed template geared towards performance and oversight. We will eliminate the transition into a monthly financial report that was included in the original guidance. The monthly report was originally intended to provide a more detailed level of reporting. But instead, we will continue the weekly financial report with enhanced

reporting requirements so that more up-to-date information will remain available for the public, Congress, and Federal managers.

To further ensure that Recovery funds are tracked and monitored to the sub-recipient and project levels, the updated guidance also provides significantly more detail on recipient reporting and establishes data collection methods, standard data definitions, and a process by which the recipient information will flow into Recovery.gov.

The guidance will clarify several points. For instance, our guidance will establish that the Administration will be able to track the vast majority of Recovery funding to the sub-recipient and project levels. For contracts, which total about \$60 billion of the Recovery Act, we will be able to track Federal contracts awarded, how prime contractors are using the funds, and information on any sub-contracts that they award.

For the approximately \$300 billion in grants that are subject to recipient reporting requirements, we will be able to collect detailed information on Federal grants awarded and sub-awards from the primary recipient. Overall, we anticipate that we will be able to collect sub-grant information in about 95 percent of the cases and we are working to expand that going into the future to collect the other 5 percent.

I would just like to stop here and acknowledge, when we came before you the last time, we heard the concerns that this Committee raised with regard to making sure that we follow this money as far down through the chain as possible. As much as possible in everything that we are doing going forward, we are trying to capture those concerns. This is a first step towards addressing some of your concerns and we are going to continue to take steps going into the future.

We are going to ensure that recipient data collection will be centralized. OMB will oversee the development of a central collection system for recipient reporting, which will lower government-wide system modification costs, improve the consistency and availability of data, and alleviate reporting burdens for the recipients by establishing the central point of collection. We are only going to make a limited number of exemptions to that centralized point, and we are going to make those exemptions for those agencies that have clear expertise or systems already set up where it might be disruptive to create a secondary system.

Recovery Act reporting will be standardized via the terms and conditions for Federal grants, loans, contracts, and other awards. This will also assist agencies in implementing Davis-Bacon and Buy American provisions.

And finally, OMB is interested in public views on this guidance and will be accepting public feedback through April 17. After this date, OMB will plan to issue another update to their guidance based on those comments from stakeholders, including Federal agencies, Congress, State and local government officials, grant and contract recipients, and citizens.

There are just a few of the things that we are trying to do to address the concerns that you have raised in the past.

To point to another issue raised by members of this Committee, the Administration is committed to ensuring that agencies have the



skills and capacity to plan effectively, award and administer contracts, and carry out programs funded by the Recovery Act. Per the advice of this Committee, we are reviewing the use of a government-wide contingency contracting corps in limited circumstances.

However, given the likelihood that the activities of the Recovery Act will require many agencies to handle an increased workload over an extended period of time, we are also encouraging agencies to use various existing authorities and options, such as the direct hire authority or coordinated interagency recruitment efforts. We are looking at all available personnel authorities that are currently available. For example, on March 17, the Office of Personnel Management (OPM) authorized the government-wide use of excepted service appointments so that agencies can quickly hire additional staff without sacrificing veterans preferences.

We are also reviewing a bill introduced by Senator Collins recently which would authorize Federal agencies to re-employ retired Federal employees on a limited basis without offsetting the annuity from salary. Employing retirees could be a promising means of building capacity for Recovery Act implementation and we are supportive of the kinds of additional flexibilities proposed in this legislation.

With that, I will conclude by reiterating that all levels of and branches of government have been entrusted with a great deal of responsibility for helping to lead the Nation out of an economic crisis. We share the burden of living up to the expectations of the American people and delivering the transparency and accountability and performance that we promised.

Thank you, and I look forward to your questions.

Chairman LIEBERMAN. Thanks very much, Mr. Nabors. That was very helpful in many regards and I thank you for responding to the concerns and questions raised by the Committee at the last hearing.

Mr. Devaney, welcome. Obviously, we have enjoyed the presence of you and your testimony before at this Committee. We welcome you in your new capacity and thank you very much for taking on these responsibilities.

**TESTIMONY OF HON. EARL E. DEVANEY,<sup>1</sup> CHAIRMAN,  
RECOVERY ACCOUNTABILITY AND TRANSPARENCY BOARD**

Mr. DEVANEY. Thank you, Mr. Chairman, Ranking Member Collins, and Senator Burris. I want to thank you for the opportunity to testify today. I have had the honor of testifying, as you mentioned, before this Committee in the past as the inspector general of the Interior Department, and as you know, the President has recently appointed me to chairman of the Recovery Accountability and Transparency Board, and it is in that capacity today that I appear before you.

I am pleased to tell you that the board has recently obtained office space and is busy acquiring a staff of highly skilled oversight and IT professionals. Our first board meeting, as mentioned earlier, was held last week and we have set in motion a number of initia-

<sup>1</sup> The prepared statement of Mr. Devaney appears in the Appendix on page 235.

tives to ensure that the board fulfills all of its responsibilities under the Recovery Act.

The members of the board, and I, view the board as having a dual mission. First, the board is responsible for establishing and maintaining a Web site, the purpose of which is not only to foster historic levels of transparency, but to do so in a user-friendly way. Second, the board will coordinate and conduct oversight of Recovery funds to prevent fraud, waste, or mismanagement.

Even before the Recovery Act was signed into law by the President, OMB and the General Services Administration (GSA) had begun designing the architecture and creating the implementation plan for the Web site. A great deal of credit must be given to OMB and GSA for their efforts to launch this Web site. Because of their efforts, all Americans can visit the Web site today, as we have talked about, at [Recovery.gov](http://Recovery.gov). However, I think it is important to point out that the creation of this Web site is an evolving process with multiple phases. It is not a single event.

As you know, the Recovery Act vested the board with the authority to maintain this Web site. Now that this first phase of getting [Recovery.gov](http://Recovery.gov) up and running is over, I am eager for the board to start the second phase of development. During this second phase, the board will begin to manage the Web site's design and content. OMB will retain responsibility for the reporting guidance and the collection and verification of data and GSA will continue to host the Web site.

I am confident that this division of labor will provide the best opportunity to maximize [Recovery.gov](http://Recovery.gov)'s use as a transparency and accountability tool, and I am equally confident that we will also have the opportunity to achieve an unprecedented level of citizen participation.

IGs across the Federal Government have developed multiple strategies to help prevent fraud, waste, or mismanagement of Recovery Act funds. In fact, this Committee recently heard testimony about some of those preventative strategies from the Chairman of the IG Council, Ms. Fong. What I can tell you today is that IGs are quickly transforming those strategies into real action. For instance, at least six IGs have finished reviews of previously unimplemented IG or Government Accountability Office (GAO) recommendations. These reviews will allow the Departments to take corrective actions now to ensure that effective controls are in place for handling these funds.

Interior Department's Office of Inspector General has developed a risk-based model to use in conjunction with Recovery grant funds and is now assisting the Department with developing its own risk-based models for grants with the hope of extending those models to contracts and cooperative agreements.

Energy's Office of Inspector General has completed over 30 fraud awareness briefings nationwide involving over 2,000 attendees. And several other IGs have audits and evaluations that are about to be released which will include recommendations that will be particularly helpful to the Departments for Recovery Act activities.

At our first board meeting last week, both Ms. Fong and I supported the board's decision to form a new Recovery Funds Working Group, which will be co-chaired by Board Member Calvin Scovel,

the IG of Transportation and a member of the board staff, former IG John Higgins, will be the other co-chair. The purpose of this working group will be to ensure a maximum level of coordination and cooperation among the IGs necessary to prevent fraud, waste, and mismanagement.

Mr. Chairman, you and the Members of the Committee have noticed that I have been using the word "prevent" to help describe the board's mission of accountability. That is very deliberate on my part. The language of the Recovery Act strongly suggests that IGs and other oversight entities are being asked to minimize the risks inherent in distributing such an extraordinary amount of money and to maximize the opportunities to prevent fraud, waste, or mismanagement in the first instance before it happens.

I see the board actively detecting fraud trends, identifying best practices for conducting reviews, designing risk-based strategies to help focus the oversight community's limited resources. The new Recovery Funds Working Group will undoubtedly serve as a catalyst for an unprecedented leveraging of resources. We will also work closely with the Department of Justice to ensure that when fraud is detected, a swift, coordinated process will follow.

Finally, I would like to talk about some of the biggest challenges I see the board having. First and foremost is the matter of data quality. Simply stated, the Federal Government's systems have never been fully successful at producing timely and reliable data.

Second to data quality is the lack of an adequate number of procurement professionals at all levels of government, not only the Federal Government. However, I am encouraged by the news that the Office of Personnel Management has tentative plans to hold a multi-agency job fair sometime in May to help agencies with their human resource needs in this arena.

And finally, Mr. Chairman, I am concerned that there may be a naive impression that given the amount of transparency and accountability called for in this Act, little or no fraud or waste will occur. I am afraid that my 38 years of Federal enforcement experience tell me otherwise and that some level of fraud or waste is, regrettably, inevitable. Obviously, the challenge for those of us charged with oversight will be to significantly minimize those losses. My promise to this Committee today is that my staff, the members of the board, and I will work tirelessly to reduce those losses to the lowest level possible.

Mr. Chairman, Members of the Committee, that concludes my oral remarks and I would be glad to answer any questions.

Chairman LIEBERMAN. Thanks, Mr. Devaney. That is a good beginning. We will do 7-minute rounds of questions.

Mr. Nabors, let me talk first about the speed with which money is being spent, because obviously one of the reasons the President asked Congress and Congress responded with the Stimulus Act quickly was to get the money out into the economy. You have mentioned some numbers, \$51 billion obligated, and then I think you said another \$151 billion, which I take it is formula money that will go out to the States.

But help put that in some context for us. The total of the stimulus package was \$787 billion, rounding off. That is over a 2-year period. In the Senate—I am pleased to say that under the way we

wrote the bill, 80 percent would be spent in the first 2 years as opposed to a lower number when it originally came through the House. Give us a sense how these numbers fit in.

Obviously, if we divide the \$780 billion by two—you tell me if this is correct—then it would seem there would be \$390 billion available this year. So how much of that would you say has begun to move out into the economy? And am I choosing the right numbers as a reference point?

Mr. NABORS. Well, I think it is a little more complicated than that—

Chairman LIEBERMAN. Yes, I would suspect it.

Mr. NABORS. If you look at what both the OMB technical staff and the Congressional Budget Office (CBO) technical staff were projecting, they were projecting a ramp-up in year one and significantly more activity at the end of year one leading into year two, and I think that is exactly what you are seeing right now.

The numbers that I talked about were just grants, loans, and contracts. Within the \$787 billion that you referenced, there is additional money with regard to food stamps—

Chairman LIEBERMAN. Right.

Mr. NABORS [continuing]. Unemployment benefits, and tax cuts. That money is not tracked in the numbers that I was talking about with regard to obligation, but that money is also making its way into the economic system, as well, so—

Chairman LIEBERMAN. And that is a substantial amount of money—

Mr. NABORS. Absolutely.

Chairman LIEBERMAN. That is many tens of billions, and presumably, as you indicated, with the reduction in the payroll tax credit, that has begun to feed in as of yesterday, as of April 1. I presume with food stamps and other programs, the extra benefits are already going out, but that they would go out over a period of time as people become eligible for those benefits.

Mr. NABORS. That is correct. The food stamp money has not yet gone out, but it will go out soon and it will go out in an even way over the entire length of the program.

Chairman LIEBERMAN. Right.

Mr. NABORS. With regard to unemployment insurance, those benefits are available through December 2009, so it is on a slightly shorter time frame than the rest of the benefits.

But I think overall, what you should expect to see is that agencies—and we are encouraging this type of behavior—agencies are taking time right now to plan their spending activities. We will see increased grants, loans, and contracts being made going into the summer and into the fall with a—and there will be increased activity going into the end of this year and going into the beginning of next year. I think that both OMB and CBO were projecting large bumps in terms of the amount of spending that is being done probably by the end of this year and at the beginning of next year. So we are ramping up to that.

Chairman LIEBERMAN. So what number do you use? I mean, the presumption was that all this money could not be spent in the first year or even in the first 2 years. What percentage of it do you hope will be spent in the first year, and if you can—I may be pushing

you to take a guess—what percentage do you think has already begun to flow out into the economy now?

Mr. NABORS. Our goal is that within the first 18 months, through this year and going into the next fiscal year, we would hope that 70 percent of the funding is actually spent.

Chairman LIEBERMAN. OK.

Mr. NABORS. And I think we are on track to accomplish that.

Chairman LIEBERMAN. OK. So that is a kind of front-loading, if you will.

Mr. NABORS. Yes.

Chairman LIEBERMAN. And that does not count all of next fiscal year.

Mr. NABORS. Well, it counts all of next fiscal year. It does not count all of the next calendar year.

Chairman LIEBERMAN. OK. So by the end of the fiscal year 2010, you hope to have spent 70 percent—

Mr. NABORS. Correct.

Chairman LIEBERMAN [continuing]. Of the money, which is a little lower than I think was originally anticipated. Is that because of the capacity of the system to spend quickly or is that just the way it ended up once Congress sent the bill to the President?

Mr. NABORS. I think that is just a reflection of the changes in programs that were made as the bill was going through conference.

Chairman LIEBERMAN. Right.

Mr. NABORS. I think that we will still have a responsible plan. I think over the period of the plan, we are still making significant investments that will—even the promise of the money will jump-start the economy.

Chairman LIEBERMAN. Yes. I understand what I am asking is very dependent on definitions, but what percentage of that would you say has been obligated now—which does not necessarily mean spent yet, but it is into the flow?

Mr. NABORS. I would want to get back to you with a more definitive answer for the record on that. I know the answers with regard to the spending side. I would want to talk to the Treasury Department with regard to some of the tax revenues that are floating out.

Chairman LIEBERMAN. But to summarize it, are you feeling good about the extent to which the system, the governmental agencies responsible, have begun to move the money out into our economy and into people's pockets?

Mr. NABORS. I do. We are still at a very early stage in the Recovery Act—

Chairman LIEBERMAN. Right.

Mr. NABORS [continuing]. And for the most part, the agencies are still in the planning phase. We want to make sure that the planning phase is as effective as possible. We are planning on working closely with Mr. Devaney to make sure that, as he mentioned, that we are trying to avoid waste, fraud, and abuse up front, and as we develop those plans, more of that money will go out the door.

Chairman LIEBERMAN. OK, thanks.

Mr. Devaney, not only do we oversee, but the press does. I want to ask you to respond to two press stories I have seen. One is the *New York Times* report that bids on some of the first stimulus construction projects are coming in lower than expected, which is good

news. But then others raised the question, particularly watching what has been happening in the area of Department of Defense acquisition, about whether the initial bids are accurate and whether there will not be inflation as we go along.

The second is a story the press always loves, and we know this from Department of Defense history, regarding spending on toilets. There is a press report that the Forest Service used an existing GSA Schedule for the purchase of 22 precast concrete toilet buildings for the Mark Twain Forest in Missouri and therefore did not solicit any other bids. My own understanding of this, and I am not drawing a conclusion about the fairness of the price, is that when an agency purchases off the GSA schedules, it does not mean there is a lack of competition.

So give us a quick response to both of those.

Mr. DEVANEY. Let me start with toilets first.

Chairman LIEBERMAN. I am not going to comment. [Laughter.]

Mr. DEVANEY. Unfortunately, the first thing that came through the door was this.

Chairman LIEBERMAN. Yes.

Mr. DEVANEY. And it was borne from a story that chronicled the first 11 contracts, actually, that were let, and so when they came to our attention—we have the ability to do a preliminary inquiry and take a look and see and identify, if, in fact, it was sloppy reporting, if something was tagged wrong, or something is not in the right database, we probably can do that. But of the 11, we ended up referring nine of those to the two IGs that had the nine contracts and—

Chairman LIEBERMAN. So they are going to follow up on that?

Mr. DEVANEY. They are going to follow up on that and get back to us, but actually, if you are going to need to do interviews in the field, they are going to have to do that.

Chairman LIEBERMAN. And there was the suggestion that by using a GSA Schedule, they were avoiding the law's requirement for competitive contracting procedures.

Mr. DEVANEY. Well, the law does not actually forbid using the GSA Schedule. It just says that it should be competitive as often as possible. The positive thing about the GSA Schedule is these companies have been vetted and they have been used before—

Chairman LIEBERMAN. Right.

Mr. DEVANEY [continuing]. And it is something that I think contracting officers will think about when they are trying to move money fast.

Chairman LIEBERMAN. So we will rely on you to let us know when you get the IG reports back.

Mr. DEVANEY. Right.

Chairman LIEBERMAN. How about a quick response to the other story about the first bids on construction coming in lower than expected?

Mr. DEVANEY. I will get back to you on that. I am really not familiar with this.

Chairman LIEBERMAN. Thank you. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Devaney, you said in your testimony that your many years of experience informs you or convinces you that some level of waste

or fraud, regrettably, is inevitable. The problem here is the numbers are so huge that even if we lose a very small percentage to waste, fraud, and abuse, it is a big number. Do you have a percentage estimate based on your experience of what you are concerned will be lost to waste, fraud, and abuse?

Mr. DEVANEY. Well, as I mentioned in my testimony, our goal is to reduce any percentage to as low as we can possibly get it, and the transparency that is going to be in this arena has never before been in place. So I am excited about the opportunity to have the force multiplier, to have citizens telling us about things that we probably will not discover if it were not for them calling in or e-mailing in that something is wrong.

So I think we have a good shot at reducing it to as low a level as we possibly can, but I have been in this business for 39 years. With that kind of money on the table, the bad guys are going to come. As we put up on Recovery.gov today, I think a series of scams that have already started, people who say, we will send you a stimulus check if you send us your Social Security number and your bank account, that kind of stuff has already started. It started 6 days after the bill was signed. So that kind of thing is almost inevitable and we are going to try to get those kinds of things up on the Web site, get the press knowing about those kind of things, point people to the right departments that can help them with that.

Senator COLLINS. The more eyes, the better, clearly——

Mr. DEVANEY. Right.

Senator COLLINS [continuing]. As I said in my opening statement. The problem is, if you take \$787 billion, even if it is a 1 percent loss, you are talking about a huge amount of money and that is why I think that it really is important to enlist citizens in reporting and to make sure that you have the resources to follow up on those tips, because we have seen cases in the past where citizens or Federal employees have called to blow the whistle on fraud and the resources have not been adequate, which brings me to your testimony today on the two biggest challenges.

The first is the quality of the data. The second is the lack of qualified procurement personnel. Mr. Nabors very kindly mentioned the bill that I have introduced with Senator Kohl that would allow experienced Federal employees who have retired to be reemployed temporarily to help meet this surge capacity need. Do you support legislation that would allow for the rehiring of annuitants without their incurring a financial penalty?

Mr. DEVANEY. Well, speaking personally, yes, I do. I do not think the board has taken a position on that, but I cannot imagine that not being a good thing.

Senator COLLINS. Thank you.

Mr. Nabors, I want to bring to your attention an issue that has come up in Maine. The people of Maine are trying hard to comply with the guidance and report accurately, but on some issues, it has been difficult to figure out exactly what OMB wants to have reported. One of them centers on the very important issue of what constitutes a job. Now, since all of us are very interested in how many jobs are created—that was a major purpose of our working so hard to pass this bill—this is an important measure of our suc-

cess. Let me give you the specific example that the people of my State have given to me.

There is a paving project that is going to be funded from the stimulus bill from Topsham to Gardiner in Maine, and it is going to create much needed jobs. Those jobs are, however, temporary jobs. They are only going to exist as long as this paving project is underway and it will take a number of months, but then it will be completed. Then those individuals, theoretically, at least, could go on to another project that is funded by the stimulus law, another transportation infrastructure project.

So how are they counted? Are they counted twice, which is not exactly accurate because it is one person continuing to have a much-needed job, but on two different projects? Are they counted twice, because, after all, they are new jobs that are created and would not exist. Are they not counted at all because they are temporary jobs? What do I tell my constituents on how to comply?

Mr. NABORS. You have put your finger on the exact issue which is sort of confounding us in terms of making sure that we have a standard way of reporting that. In the very near future, OMB is going to be putting out specific guidance with regard to how to calculate the job numbers. We are working very closely with the Council of Economic Advisers (CEA) so that we have the best economic measures and the best economic minds thinking about this so that we can standardize those types of issues across not just States, but also across Federal programs, as well.

Just to give you one example, building on what you have just said, we will get estimates from the Department of Transportation, who is very familiar with the type of issue that you are raising. They use a calculation for job years. Well, job years is not the same as a job that the Department of Energy is calculating. What we are trying to do right now is come up with a methodology so that it can be standardized in such a way that everybody can use it in the same way, but most importantly, that it does not misrepresent the numbers.

I think that you are absolutely right. The whole reason for the Recovery Act was to create or save jobs. I think the last thing that we want to do is misrepresent what is actually going on with the dollars that we are spending. So within the next few weeks, you should see that guidance coming out and we hope that it will be helpful to States and local governments in terms of making those types of calculations.

Senator COLLINS. Thank you. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Collins. Senator Burris, good morning.

#### **OPENING STATEMENT OF SENATOR BURRIS**

Senator BURRIS. Good morning, Mr. Chairman, Ranking Member Collins, and to our distinguished presenters.

My question will initially piggyback on what Senator Collins was asking in reference to the ability to bring in talent, Mr. Devaney, from the other governmental employees. Do we have a number, in terms of these agencies, of what we are really looking for in terms of the number of personnel? And second, I would assume that these agencies with the stimulus packages have been provided resources



to handle that, what size are we talking about in terms of costs in that regard?

Mr. DEVANEY. Well, Senator, I think that it is fair to say that this is a problem across government. It is not any particular agency. It is absolutely across the board. There has been not much hiring in the procurement professional arena over the last decade, and at the same time, there has been flat hiring. There has been an awfully big increase in spending and this bill just dumped on top of that is causing a great deal of concern.

IGs are looking and working with the departments to see what the gaps are, what the needs are. The board is required to conduct a review, which we have just started, to look and see what the needs are and what the situation is. I think as of 2 days ago, and now up on Recovery.gov, the first report came out of the Department of Energy, which suggests that they are understaffed in the procurement professional arena. Even though they have actually undertaken a hiring blitz over the last 3 or 4 years and gone up in percentage, still, with this kind of money going to be spent, they are going to need to do better. We have an aging workforce. We have people eligible to retire. So all of this is sort of coming together as a perfect storm, if you will, and it causes me great concern.

I think OPM is looking at a number of different kinds of solutions, and as I mentioned in my testimony, they are going to hold job fairs. But I think they are going to do a lot of thinking about issues like Senator Collins raised with retired annuitants and other things to bring some relief to this very troubling area.

Senator BURRIS. Mr. Nabors had mentioned the fact that there are \$51 billion that has either been obligated or is already out there, and I would assume that we are tracking that pretty closely, if either one of you all want to respond to that, in terms of are those dollars in advance of our tracking system? We need to make sure that they are going to get the same scrutiny that dollars will be 6 or 7 months from now.

Mr. NABORS. No, they are not in advance of our tracking system. Right now, we currently have a system in place where the agencies are reporting to us on a weekly basis on their financial activities. Grant information, contract information is coming to OMB and we are making sure that information is made public. A lot of the initial funding are obligations related to things like Medicaid and we have a very good idea on where that money is going because it is largely going to States for health care types of costs.

Senator BURRIS. Now, are you sure the States are geared up? Will your computer be able to track down to the spending point of that contract or of that grant from the States?

Mr. NABORS. The guidance that we are going to put out tomorrow will put in place a system that will allow us to track sub-contract recipients.

Senator BURRIS. Mr. Devaney, I think about the fraud issue and abuse issue, and being a former attorney general of my State, would certainly say that you have to look for those type of resources, especially your State attorneys general that could help you with that fraud and abuse tracking process, and I hope that there would be some attempt to bring those in, especially as a part of the

overall tracking system. Will this put an additional burden on the State resources?

Mr. DEVANEY. Absolutely, Senator. I think what we are looking to do is we are going to have in-house an experienced prosecutor that is going to work at all levels of government, Federal, State, and local, with district attorneys, attorneys general, and try to figure a way to leverage our resources, to figure out how to best present fraud awareness training and to help prosecutors at all levels of government.

Senator BURRIS. But you know what will be reported, the sensational story where the one person got away with a major contract, and they are out there. They are trying to do it. It is amazing how the schemes come about. You mentioned it already, they are already advertising with their schemes to try to rip off the government. We spend more money trying to protect ourselves, which will then free up a lot of money to get out from people trying to rip us off.

So I just hope that we are able to track this, because as Senator Collins said, that is a lot of money when you are dealing with these numbers and these sizes. If you are just talking about a tenth of one percent of a few billion dollars, the taxpayers are going to start looking at all of us, saying, why did not we do something?

Of course, we have to make sure that we do what the President said we are going to do, which is that we are going to watch every dime. I hope that we can probably watch every \$100 million rather than every dime, because if we can watch every dime in this, I want to know what format President Obama is going to be using and I would want to commend every staff member on your team and on Mr. Nabors team who protect our money. I mean, you all should get a major blue ribbon for that.

Mr. DEVANEY. Thank you, Senator.

Senator BURRIS. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator Burris. Senator McCaskill, welcome.

#### OPENING STATEMENT OF SENATOR MCCASKILL

Senator McCASKILL. Thank you very much.

I know we are struggling with overseeing some of this money and the last time we talked a little bit about the Single Audit, I heard back from most of the GAO and IG community on it and I completely understand that we cannot abandon some of the basics of the Single Audit, primarily the financial statement audit, because everybody depends on that for their bond ratings. And we have to have a schedule of expenditures in terms of Federal awards just so everybody can keep track of who has what.

But the requirement that 50 percent of all Federal funds be covered and the emphasis on the very large low-risk programs, the A-level programs, as opposed to, for example, in my State, and I think in all of the States, where we are going to have some ugly stories before this is all over is in the Weatherization Assistance Program. I look at the Urban League of St. Louis, and typically they get a million dollars a year for weatherization programming. They are going to get \$15 million.

Where do these crews come from? Are they competent to do the work? Has it been bid? And are they being told it is OK to turn the money back in instead of the alternative of giving a second cousin who has a pick-up truck and two friends a bunch of money to go weatherize some homes, and then we go and check and maybe they put weather stripping around the front door and that is all that happened.

I mean, we are up here, and you get right down to it, I think the home Weatherization Assistance Program is not like Medicaid. It is not like child support. But it is one of those places where you have a low-level program that now has incredibly high risk because we are overloading that program with a whole bunch of money they have never had before.

Where are we on looking at the OMB annual Compliance Supplement A-133 and what chances do we have of changing it this year to move out some of these A-level low-risk programs and get at some of these smaller programs where I think we are going to have some problems?

Mr. NABORS. Well, in response to your comments from the last hearing and in response to your letter, I have asked the OMB staff to work with the key stakeholders to determine how the Single Audit process can maximize the accountability and transparency of our Recovery actions. By the end of April, OMB is planning on publishing an update to the compliance supplement for Circular A-133 and this will clarify the coverage of the Single Audit. It will highlight significant accountability requirements for Recovery dollars and it will help to ensure that appropriate Recovery programs are designated as high-risk and audited as major programs.

Senator McCASKILL. And they are looking at this, the issue that I talked about—

Mr. NABORS. Absolutely.

Senator McCASKILL [continuing]. Where we are putting a bunch of money—I mean, a lot of these programs are going to get looked at anyway, but when you have such a huge bump-up, that is where I think—

Mr. NABORS. And if I may, ma'am, you will know more about Circular A-133 than I will ever know and I was hoping that I could have my staff come up and work with your staff as we put together this supplement—

Senator McCASKILL. That would be terrific.

Mr. NABORS [continuing]. To make sure that we are, to the extent possible, capturing the concerns that you have.

Senator McCASKILL. That would be terrific. And what might be really helpful is to get somebody on the phone in a conference call at that time that actually does an A-133 audit in the State. There are people in every State that take on this responsibility to do these audits, the practitioners at the State level, and the government auditors at the State level.

And I would think pulling together two or three of those people—I am not talking about the elected State auditors or the appointed State auditors. I am talking about, I mean, there was somebody in my office that had been doing the Single Audit, responsible for 20 years. They know everything. Frankly, they know a whole lot more about it than I do.

And I think getting those kinds of practitioners together quickly is important, and you could do it very easily through the State auditors association. You could pull together five or six very senior State auditor practitioners, not the bosses, but the worker bees, the ones that are actually going to do the work papers and the ones that are actually going to look at internal controls and all those kinds of things that those of us who hold the press conferences do not do.

Mr. NABORS. We will do that.

Senator McCASKILL. OK. Let me also ask you about the Federal Audit Clearinghouse for Single Audits. This is going to be a great location because I think all these State auditors, regardless of what you do with A-133, are going to want to look at these funds because there is a lot of political pressure for them to look on these funds, although a lot of State auditors are not elected. But having said that, most of them are going to feel the pressure to look at this money and how it is being spent.

Typically, the Federal Audit Clearinghouse is not really particularly well-suited for the average citizen. It is not really user-friendly. And auditors—and I know that Mr. Devaney will back me up on this—many times, they do not speak English. They are a little bit like the people that hang out at the Pentagon. They have a lot of terminology that is not friendly for the average person.

Have you guys on the board considered looking at the Federal Audit Clearinghouse and seeing if we could incorporate that into Recovery.gov, because it is going to be a great treasure trove of oversight information on the stimulus money and it seems to me we ought to transplant that over to Recovery.gov in a user-friendly way that allows people to get to their own State audits to look at what is actually happening in their States in terms of oversight.

Mr. DEVANEY. Senator, I think that is a great idea. I mean, we really had not thought about it, but I appreciate you bringing that up and I fully agree that whatever we do, it has to be in English and not “auditesese.”

Senator McCASKILL. Yes. And speaking of English, we have been spending a lot of time on Recovery.gov in my office and the weekly updates, kind of feel like internal use project plans. They do not feel like they are being written so people can look at it and really understand what is happening. I do not think they are useful to most people, the weekly updates, the way the terminology is and the way it is characterized.

Let me ask you this. On Recovery.gov, do you have folks that are like the people who go into the restaurant that are working from the newspaper and going to see how well they do with their food? Do you have people accessing this Web site and giving you objective third-party feedback that are not working there in terms of what they are learning, what they are not learning, and how it works?

Mr. NABORS. Well, the Recovery.gov does have a link that allows the public to comment and add suggestions with regard to how we are performing. But I would defer to Mr. Devaney.

Mr. DEVANEY. Well, every morning, Senator, I get up and I go to Recovery.gov, the first thing in the morning, and I share your concern.

Senator McCASKILL. You poor thing.

Mr. DEVANEY. I share your concern. Well, it is mine, so I——

Senator McCASKILL. I know it is yours. [Laughter.]  
You have no choice.

Mr. DEVANEY. I have no choice. But let us say it this way, that the site, as I mentioned earlier in my testimony, is an evolving process and this site is going to be, I believe, an opportunity to really have an historic level of transparency and citizen participation, and it may serve, if we do it right, as the model for how we do this in the future.

And so I am determined to get this right, and I think, for instance, content management is an issue, that we are now transitioning from OMB's good work standing this site up to the board is going to take over content management, and I am working very hard to get on my staff people who can write in English and can put stuff up to which people are going to be attracted. And at the same time, the technology out there, it is phenomenal, what we can do with this site. In a relatively short time, I think we can have a site where people would only go on it once, but want to come back the next day and the day after because we will be able to drill down as the information starts coming back in to the level where people really want to see this in the neighborhood.

Senator McCASKILL. Thank you, Mr. Chairman, for your indulgence. Let me just say that I think another idea I would give you is that I discovered that the best thing I did when I was an auditor was I hired a journalist to begin writing the summaries for audits. Unfortunately for our democracy, there are a lot of journalists looking for work right now and they understand how to write a lead, they understand how to keep it very concise, they understand how to make it interesting, and I would certainly encourage you to look at the vast number of really qualified journalists that are out there looking for work right now because I think you could get some real talent that could really help us with that content in terms of making it interesting to people.

Mr. DEVANEY. Senator, tomorrow morning, I am interviewing two journalists.

Senator McCASKILL. There you go. All right. Great minds think alike. Thank you, Senator.

Chairman LIEBERMAN. Thank you, Senator McCaskill. Senator McCaskill has her own stimulus employment program. [Laughter.]

Senator McCASKILL. Helping all the people out there typing on their laptops.

Chairman LIEBERMAN. I appreciate that.

We will do a second round if people want to stay. I think we have a while before the vote-a-rama starts.

Let me just pick up on the Web site, if I might. The usage is really miraculous or stunning. So to the extent that you are analyzing now, am I correct in assuming that most of those hits are just looking for information about how the stimulus works, how you might get funds, or something of that kind?

Mr. DEVANEY. Mr. Chairman, I think people are coming in right now out of curiosity——

Chairman LIEBERMAN. Yes.

Mr. DEVANEY [continuing]. And seeing what is there. And what I would say to them is keep coming back periodically and I think you will see it getting more robust and more user-friendly. And I am really excited about the idea. There are some terrific technologies out there that we can use, interactive mapping and drill-down techniques where you can get down to where I think people really want to see the rubber hit the road. And I think OMB's guidance coming out now will be very helpful in getting down to those lower levels that you have expressed some concern about.

And then we need to display that. We need to be able to let people go on that Web site, click on their State, and then keep clicking until they get down to their city to see the projects, to see the money that has been spent in that area——

Chairman LIEBERMAN. Yes.

Mr. DEVANEY [continuing]. And all of that is possible. It is not there now, but it will be.

Chairman LIEBERMAN. I appreciate that commitment to make that happen.

Let me ask you about the extent to which this is interactive. For instance, tell us about the process—it is early on now in the program, but this will presumably happen—where someone will say, hey, this Stimulus Act money in my town is being used badly, or my company got a grant and it is being wasted. How do you funnel those comments to a point where you can respond to it and use it?

Mr. DEVANEY. Well, if the call were to come to us, we would do what we always do in any IG office. We would get as much information as possible and then, in our case, we are going to be funneling that to the appropriate IG and then asking that IG to get back to us.

Chairman LIEBERMAN. So is there a clear portal for people to go to on the Recovery.gov Web site if they want to whistleblow?

Mr. DEVANEY. There is a portal where they can make comments. There is a portal where they can tell a story, if they wanted to.

Chairman LIEBERMAN. Great.

Mr. DEVANEY. I do not think we necessarily are, from the oversight perspective, interested in the stories as much as we are the citizen that might look across the street and see the Web site, says a school is going to be built and they look across and there is just a forest.

Chairman LIEBERMAN. Yes.

Mr. DEVANEY. So we are going to have to develop the capacity, and this is no easy endeavor, to sift through the millions of citizen comments that are going to be coming into this Web site.

Chairman LIEBERMAN. Yes, that is what was on my mind. It is pretty hard to do that right now, I assume.

Mr. DEVANEY. No, we cannot do that right now, and we are talking to groups that suggest they can do that for us. But we want to make it real. Personally, I believe that we will lose the value of citizen participation if they do not think they are heard.

Chairman LIEBERMAN. I agree.

Mr. DEVANEY. And so if you write into the site and you never hear anything back or you never see any action, I mean, that is actually worse than inviting them to do it in the first place.

Chairman LIEBERMAN. Yes, I agree.

Mr. DEVANEY. So we have an enormous challenge here. I am trying to get the smartest people I possibly can to come in and talk to us about this. It has never been done before at this scale, so—

Chairman LIEBERMAN. Right. That is a real challenge, and so we wish you well. I could not agree with you more that people at least have to have a kind of automatic response that you got their message and somebody will go over it. But to ferret out of all that input the whistleblowing that you really do want to know about is your challenge.

Let me go to a second part of this, on the prevention part. What will your IGs do—what kind of systems will they set in place, not just to detect but to prevent, with a program this large and with this money moving out this quickly, to prevent waste, fraud, and abuse?

Mr. DEVANEY. Well, as I mentioned earlier, we have created a working group where we are all going to talk to each other on a regular basis. We are going to try and leverage our resources. There are going to be some IGs that are going to be able to easily handle the load and then there are going to be some IGs who do not have the staff to do it, so we are going to have to leverage resources and achieve the highest level of cooperation, perhaps, we have ever seen before in the IG community.

And I think IGs are, right now, they are out there giving fraud prevention awareness training to the Department staff. They are out there talking to local enforcement and prosecutors. They are doing a lot of that right now. They are developing risk models, as I mentioned in my testimony. We have to figure out what the risk models need to look like in this endeavor so that we can focus our limited resources in the right place. A model that suggests that this particular kind of a grant or this particular kind of a contract, if we only have a certain amount of resources, let us expend it there.

But IGs are not just doing that internally. I mentioned at my former office, they have taken that risk model that we have always had internally and they shared it with the Department and they are encouraging the Department and working with the Department to help build their own risk models. So IGs are out there right now working with the Departments, who, by the way, are working, from my overview, very well in setting up their own internal shops to manage this money, as, quite frankly, I have never seen them do before. So I am encouraged by that.

Chairman LIEBERMAN. That is good news.

Mr. Nabors, let me ask you this question, and it may be hard to answer it now, but perhaps as we go on in this experience, when you come back, you can help us with it. Obviously, we appropriated this enormous amount of money because we all heard about the trillion-dollar gap in normal demand in the economy and we are trying to fill it and get economic activity going again.

There has been some encouraging news lately. And obviously the discouraging news is that the economy continues to bleed jobs. The encouraging news is that there was some evidence last month of consumer spending going up a little bit, of more activity in housing sales, and the stock markets had their best month in March in quite a while.

So I do not know whether you have any ability to relate that to the money that the Recovery and Reinvestment Act has put out into the economy thus far. I would welcome that analysis as we go on, which is a way in a broader sense for us to try to determine whether the Stimulus Act is achieving its purpose.

Mr. NABORS. We do not have it now, but I would be happy to work with our staff to generate that model for you.

Chairman LIEBERMAN. I appreciate it. I mean, it is hard to imagine that putting this much money out into the economy would not help some. I mean, the question is, how do we track, to the best of our ability, how much it has helped? I thank you.

Senator Collins.

Senator COLLINS. Thank you.

Mr. Nabors, I want to bring up another area that really concerns me, and that is when the omnibus appropriations bill was passed, without my support, I would add, it did not reconcile the funding in that Act with the funding that we had just approved a couple of weeks earlier as part of the stimulus bill. The result is that there are some Federal agencies that are going to receive an enormous increase in funding, far beyond what they have ever handled before. Let me give you a specific example.

The Federal Railroad Administration (FRA) has traditionally been a very small agency that is responsible for dispersing some Amtrak funding. Now, its funding is going from \$1.5 billion to over \$10 billion. It is an enormous increase in the funding that this very small agency is going to have to get out the door properly in grants and contracts. Are you doing anything to target agencies like this one that are receiving, as a result of the combination of the Stimulus Act and the omnibus bill, a massive increase in funds but may not have the people and the procedures in place to ensure the money is spent wisely?

Mr. NABORS. This issue is one of the primary issues that we have been focused on since the passage of the omnibus, making sure that there is the appropriate management and planning structure in place, especially for these agencies that are not used to seeing large sums of money. The Vice President has been very involved personally with regard to the FRA and ensuring that they have both the personnel and the plans and procedures in place to ensure that this unprecedented amount of money that was provided to them is used for what it is intended, and that is to both stimulate the economy and to fundamentally transform the way our infrastructure system operates in this country.

It is going to be a challenge. I will not try to softball that one. And it is a challenge that we are dealing with each and every day. But it is something that we are all very cognizant of and it is something we are focused on and it is something that we are working on every day.

Senator COLLINS. Mr. Devaney, are you giving extra scrutiny to agencies or programs that have had massive increases in funding? It seems to me that this is a recipe for the kinds of problems that you have been talking about.

Mr. DEVANEY. I think you are right, Senator, and I think this IG Working Group that we have put together, all of those IGs, as I mentioned, are at some stage in developing risk models and the



kind of things you are talking about would be the kind of agencies we would look at as high-risk. And so I think what you will see emerging at some point is a strategy for IGs, maybe somewhat different in different Departments, but overall, we are going to try to identify those high-risk areas. That one would certainly be one.

Senator COLLINS. Mr. Devaney, you talked earlier about the e-mail scams that are already going around——

Mr. DEVANEY. Right.

Senator COLLINS [continuing]. And one of them asks people to send personal data and information in order to get their “stimulus check.” I am fearful that a lot of people will fall for that scam because—and what I think was an error in policy—we did do these one-time checks a year or so ago of \$300 or \$600 to taxpayers. So this may well ring a bell with the citizens of this country and they may respond to it.

Have you thought of enlisting groups like AARP, or there is a group called Triad that works with local prosecutors to try to educate seniors in particular? It is fine for the IGs to be aware of this. It is fine for the Federal Trade Commission (FTC) to put out alerts, but that is not going to reach a lot of people who will receive these e-mail scams. It seems to me that you need to get nonprofit groups, senior centers, Area Agencies on Aging involved. Is there any attempt to do that underway?

Mr. DEVANEY. Not yet, but that is a wonderful idea. I mean, we have just been collecting all the various scams. We put them up, I think, 2 days ago on Recovery.gov and we have been working with the various agencies like FTC and we have all of the linkage. On Recovery.gov, we have links to all of those agencies. We have links to all the IGs at the respective agencies. But working with groups like AARP, that is a wonderful idea. We will do that.

Senator COLLINS. Thank you.

Let me just end with one final question, and that is to go back to the issue that waste, fraud, and abuse is inevitable. I know there was a *Wall Street Journal* interview that you gave in which you expressed your concern that there could be as much as 7 percent of the stimulus funds lost to waste, fraud, and abuse. When you are talking about \$787 billion, I think that amounts to something like \$55 billion.

I just want to get on the record that we simply cannot allow that. That is an unacceptable percentage no matter what number it is applied against, but when we are talking about a number this large, the economy will lose significant funding. The public will lose significant confidence in what we are doing if more than \$50 billion is lost to waste, fraud, and abuse. So I believe it is incumbent upon all of us to ensure that does not happen.

I know what you are saying, and you are applying more than 30 years of Federal law enforcement experience to this job, but we have to ensure that does not happen.

Mr. DEVANEY. I totally agree. The 7 percent comes from a very reputable and well known association of fraud examiners, and I was asked about the 7 percent and it is \$55.1 billion. I was horrified when I first did that math. I am very hopeful that we would never, ever see something like that, but we have to get it down to the lowest level possible. I do not even like talking about the 7 per-

cent because I do not want to acknowledge it ever could be that way. It is a number that is out there.

Senator COLLINS. Thank you.

Mr. Chairman, I want to commend you for the hearings we are holding because I think that the ideas that we are all generating and passing on to you in this collaborative effort will help to ensure that we do not see that level of waste, fraud, and abuse, so thank you for your leadership.

Chairman LIEBERMAN. Thank you, Senator Collins. Thanks for your contribution in that regard. Too often we authorize, we appropriate, and then we leave the rest to the Executive Branch. This is really too critical, too big, and as I said at the beginning, it is too big for us to let it fail. So together, we have to make it work, and I thank you.

Senator McCaskill.

Senator MCCASKILL. I would like to talk a little bit, Mr. Devaney and Mr. Nabors, about blanket purchase agreements and utilizing the catalogs of existing deals. The toilets that have been talked about are in the Mark Twain National Forest and they are in my State, so I have spent a lot of time going through it, and you know what? It was not a bad deal. It made a great headline, and my friend, Senator Coburn, before you talk about the toilets, make sure I get you this memo because you will be impressed.

In reality, what they did was they looked carefully to find the least expensive way to build buildings for toilets that are accessible, low maintenance, and a good value in the Mark Twain National Forest. But because they were toilets and it was a lot of money, all of a sudden, everybody got the vision of the gold hammer and the \$5,000 toilet seat.

But it brings me to an issue that I am wondering if you all have talked about, and that is I was surprised when I got here and I learned that agencies were soliciting other agencies to buy off their book of contracts because they got some kind of bump for it. In the Armed Services Committee we were looking at this. There was actually advertising by one agency saying, use our existing contracts to buy off of because, I guess, there is some kind of transfer of funds between the agencies if they use each other's. So when GSA sells stuff to the Department of Defense (DOD), they were able to get some extra money.

Have you all looked at that in terms of these transference of funds between these agencies using existing contracts because that is not what we meant this money to be used for.

Mr. DEVANEY. Well, I would just tell you that as the IG of the Interior Department, I wrote some rather scathing reports about the use of the franchise funds at Interior. I think the Interior Department is one of seven departments that actually has that capacity. Things have gotten a lot better. They still have it, and some of the abuses that we chronicled have been corrected. But nonetheless, there are seven entities—I think there are only seven—that allow other departments to come in and they will buy you and take a piece, if you will, of the action—

Senator MCCASKILL. Right.

Mr. DEVANEY [continuing]. In some administrative fees. My critiques went to what they were doing with those fees after they got them.

Senator MCCASKILL. Right.

Mr. DEVANEY. But nonetheless, it is legislation that was passed by Congress and they are allowed to have it.

I really have not thought about these funds with those systems. I am interested to hear that is happening and we will look into it.

Senator MCCASKILL. Yes, because I think it is a place where we could have some abuse—

Mr. DEVANEY. Right.

Senator MCCASKILL [continuing]. Because there is a lot of money being put into the system and because—and, of course, they have two masters here, all these agencies. One is to get the money out quickly and one is to make no mistakes. Well, those are two masters that are hard to serve at the same time. So I think that might be something we want to look at.

Let me also, just briefly, ask you about leasing versus construction. One of the things I discovered is that we have this bad habit of leasing non-permanent buildings that eventually turn into permanent buildings that we buy. Is there any incentive in the way that we are putting this money out there that people would begin to engage in buying temporary buildings? Army Materiel Command did a temporary building, OK. Well, I went to the temporary building, and believe me, this is not a temporary building. This is a large office building, and they tried to tell me, well, we could take it apart if we needed to.

But I am curious if you all have put any rules in place about uses of this money for capital as to whether or not people are going to lease temporary buildings or if they, in fact, are going to invest in buying buildings, because right now, construction costs are so low, they might even be lower than what we would pay to lease a temporary building which inevitably the government ends up getting around to buying at the end of the day. Have you all talked about that or looked at that?

Mr. DEVANEY. We have started talking about it. I think that one of the first 11 contracts that we were asked to look at, particularly as Chairman Edolphus Towns on the House Oversight and Government Reform Committee asked me to look at, involve such a matter, and so we have referred that to the GSA IG and we are waiting for them to get back to us. But I think we want to learn from that what the scope of that problem might be.

Senator MCCASKILL. Yes. I think you are going to see—because these manufacturers can come in and do a pretty good sales pitch on temporary buildings. I am just worried that it will be a very seductive process, that people will say, well, we can just go for this lease of a temporary building. We do not have to jump through all the hoops that we would have to if it was a capital expenditure because we can take it out of a different fund, and with this stimulus money, I think that is another area that we might have some abuse. So I would appreciate any feedback we could get on that.

Mr. DEVANEY. Absolutely. Sure.

Senator MCCASKILL. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you very much, Senator McCaskill. Senator Coburn, welcome.

#### OPENING STATEMENT OF SENATOR COBURN

Senator COBURN. Thank you, and thanks for having the hearing and thank you all for coming to testify. I have read your testimony.

One of the problems that we have in the Federal Government is Congress telling us how we budget, because outside of the stimulus package, we lease almost 90 percent non-military buildings. We do that because the accounting rules we have charges the whole cost of the building in the year in which you take occupancy to the agency. So we do not actually buy. We lease because it is the least budget-impacting, which is silly and something we ought to change in the long run.

I was not prepared to talk about toilets this morning, so I will pass on that one.

Senator McCASKILL. I knew it was coming some day. [Laughter.]

Senator COBURN. Maybe, maybe not. We are looking for the truth, not the headline.

Mr. Nabors, I have some real concerns with what you all are doing thus far, and let me explain. If you go to Recovery.gov and you put another computer up right next to it and go to USAspending.gov, you see two totally different approaches. In USAspending.gov, you can go by city, you can go by contractor, you can go by grantee, you can go by Department, and you can go all the way down to find out who is doing what. I am waiting on a letter to come back from OMB now clarifying when USAspending.gov will include subgrants and subcontractors. Senator McCaskill and I were significantly involved in getting that done.

I am hearing that you plan to move USAspending.gov to Recovery.gov, which scares me to death based on what I see in Recovery.gov. Recovery.gov is not searchable where as USAspending.gov is searchable.

So would you mind settling me down a little bit in my worry and gray hair accumulation that you are going to go toward something like USAspending.gov, that is multi-searchable, that you can use almost any matrix to get where you want to go, and you can do it quickly? I spent 10 minutes this morning on Recovery.gov, and I want to tell you, there is nothing there. I know it is early, but I just want to know where you are going with it. If you are going in the direction of what it looks like versus what is on USAspending.gov, you are not going to give anybody the assurance of anything in this country about really finding out what is going on across the street.

Mr. NABORS. Well, let me try to save your gray hairs.

Senator COBURN. OK. Thank you.

Mr. NABORS. Our plan—I think it is a misunderstanding with regard to what we are trying to do with Recovery.gov. The reason why we did not use USAspending.gov right now is because there seems to be such an overwhelming demand to get information as quickly as possible onto the Web sites. The data systems that feed into USAspending.gov just are not at the point right now where we can get information up as quickly as we believe that the public is demanding it.

But our goal in the long term is to try to merge the best of both Web sites, the data quality and the extensiveness of the data on USAspending.gov along with the search capabilities with the speed that we are trying to build into Recovery.gov. Recovery.gov, in my wildest dreams, will become a model for being able to update our financial systems to a degree where we are not just able to track Recovery Act spending in almost real time, but we can also do the same types of things with regard to overall Federal spending.

I know that the Recovery Act has a special place in our economy at this point, but I think that both you and the President share the joint objective that every dollar that the taxpayers provide to the Federal Government for spending is special, as well, and we need to be able to track that money quickly. So we are trying to not necessarily bring USAspending.gov into Recovery.gov, but to learn lessons from the two to make a Web site going into the future that allows us to better track Federal spending.

Senator COBURN. What is the difficulty with getting the data? My understanding was the difficulty with getting the data to USAspending.gov is that the agencies were not providing it.

It was not a technical problem. It is that the agencies refused on a timely basis to bring it forward. If they did, how is that going to be any different on Recovery.gov using the same agencies?

Mr. NABORS. Well, the batch processing and the financial data that we use for USAspending.gov does have a significant delay and we are trying to, at this point, speed up the extent to which data is available. So we are actually using not just financial data on Recovery.gov, but potentially budgetary data and other types of information, as well, to get that money out ahead of the normal time frames that our financial systems produce that amount of information.

Senator COBURN. Right. Mr. Devaney, thank you for your years of service as IG. It is often times an unthankful job, but I know you have done a great job there and I appreciate it.

The 7 percent figure bothers me, but the 10 percent figure on the Federal Government bothers me even more. If we look at what the Federal Government is doing in total, if you come in at 7 percent, that is not acceptable, but it is better than what we are doing everywhere else. What we ought to be doing is redoubling our efforts to where we get that down to about 2 or 3 percent because after that there are diminishing returns on the dollar. I have heartburn over the \$787 billion. I have heartburn over the \$55.1 billion. However, I do not think it is going to be in better hands than in your hands to see if we cannot limit the waste.

I would suggest, besides what Senator Collins said, put Ad Council ads on TV for seniors about these scams. I mean, it does not cost much. You can get it out faster than AARP can. Two weeks from now, you can have 2 or 3 weeks' run of Ad Council ads where almost every senior in the country knows, do not fall for this scam.

You may have covered this prior to me coming in. When do you foresee that we will actually have a viable and multi-searchable Web site on Recovery.gov?

Mr. DEVANEY. Senator, we have been doing an awful lot of meeting on this, and we have been talking to a considerable amount of smart people. We are going to try to hold an electronic town hall

in the near future where we solicit the public in general and technology folks in general, and then move quickly after that with the help of perhaps somebody like the National Academy of Public Administration (NAPA) to select some vendors. There is some really amazing stuff out there that I think is going to make this site very exciting to go on. So I hope you will continue to visit it as we try to make this thing something that people are going to want to come to on a regular basis and allow them to understand where their money has gone.

Senator COBURN. If we are a year from now, and a year is a pretty fast pace to do something like this, a year from now we will have spent about 70 percent of that money already. Can we do that within a year? Can you get it done within a year? I am talking the real deal, up where people can really use it?

Mr. DEVANEY. Yes, I think we can. That is my goal.

Senator COBURN. Would you be so kind as to keep this Committee advised if you are going to fall behind that schedule—

Mr. DEVANEY. All right.

Senator COBURN [continuing]. So that if it looks like you are not—we spend \$64 billion a year in this government on IT. Thirty-six billion of it is wasted. The American taxpayer needs to know that. Thirty-six billion, over half of what we spend on IT, gets wasted every year. This is the one place where we should not waste and there should not be a hiccup. We do not need another Harris Corporation Census no-bid contract that does not perform that we paid a bonus for.

And Mr. Chairman, I would ask that my statement be submitted for the record.<sup>1</sup>

Chairman LIEBERMAN. Without objection.

Senator COBURN. And I thank you all.

Chairman LIEBERMAN. Thanks, Senator Coburn. Very good questions.

Thanks, Mr. Nabors and Mr. Devaney. I think it has been a very constructive exchange. I appreciate what you are both doing, first to spend the money that we have appropriated because that is why we appropriated it, to get it out to help the economy grow and to protect and save millions of jobs. And second, to make sure with every human and technological resource we have that the money really is spent for the purpose for which it is intended and not wasted or lost to fraud in any way. So I thank you.

I found this so constructive, and Senator Collins did too, that we are going to ask you back for a repeat performance because we really want to keep this going. We hope you find it as productive as we do. We will probably ask you to come back sometime later in May, so you have a little more time to see how it is going.

We will leave the record of this hearing open for 15 days for additional questions or statements.

I will just end with thanking both of you. You are really both very impressive public servants and we need you to do what you are doing.

The hearing is adjourned.

[Whereupon, at 11:33 a.m., the Committee was adjourned.]

<sup>1</sup> The prepared statement of Senator Coburn appears in the Appendix on page 229.

**THE AMERICAN RECOVERY AND  
REINVESTMENT ACT: MAKING  
THE ECONOMIC STIMULUS  
WORK FOR CONNECTICUT**

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**TUESDAY, APRIL 7, 2009**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Hartford, Connecticut.*

The Committee met, pursuant to notice, at 10 a.m., at the Learning Corridor, Greater Hartford Academy of the Arts, Theater of the Performing Arts, 359 Washington Street, Hartford, Connecticut, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.  
Present: Senator Lieberman.

**OPENING STATEMENT OF CHAIRMAN LIEBERMAN**

Chairman LIEBERMAN. This hearing of the U.S. Senate Committee on Homeland Security and Governmental Affairs will now come to order. Let me thank all of you for being here.

I want to apologize to all of you out there on behalf of the witnesses that their backs are turned to you, but such is our custom in the U.S. Senate.

Let me also quickly but quite sincerely thank Eric Bernstein, Principal of the Hartford Academy of the Arts, for hosting this field hearing; and Jim Keller, Managing Director of the Theater of the Performing Arts, for handling the logistical arrangements. And let me give a particular welcome to the students and teachers of the Greater Hartford Academy of the Arts and the Greater Hartford Academy of Math and Science.

[Applause.]

Let me welcome also everyone else who has come, including some in State and local service who are here to join us in what is a continuing series of hearings that our Committee is holding. The first two occurred in Washington DC. This is the third one, a field hearing here.

And the basic goal we have is to monitor how the billions of taxpayer dollars that the President requested and Congress approved for the so-called stimulus program are being spent.

I thought because the students are here I would take just a moment to give some history and explain why we are here and what this Committee is about, and maybe I will start with a personal story.

Shortly after I was elected to the Senate in 1988, I was down in Washington for some orientation meetings for the new senators, and I was at a reception, and Senator John Glenn, who was then the Senator from Ohio—and, of course, world famous for being an astronaut—came over to me and he said, “Joe, I am going to try to return a favor to you that was once done to me.” He said, “Just after I was elected, I was at a reception somewhat like this, and the then-Senator from Connecticut, Abraham A. Ribicoff”—probably the students do not remember that name, which should inspire some humility in people like me, but others will remember our former governor and Senator from Connecticut. Senator Glenn said, “Abe Ribicoff came over to me, and he said, ‘John, you are going to have the opportunity to select what committees you want to be on. A lot of times, people do not think about the Governmental Affairs Committee, but it is an extraordinary Committee. It has the responsibility, among other things, to oversee the expenditure of Federal money and to monitor what every department of the Federal Government is doing and to hold investigations’”—which, over history, the Committee has done. These investigations go back to Senator Harry S. Truman, when he investigated, during the Second World War, the spending of money during wartime. There were other investigations held by the Committee. Probably the most famous, when I was a kid, was done by a Senator from Tennessee, named Estes Kefauver, into organized crime. It goes on and on.

Senator Glenn said, “Why do not you put your name down for it? I do not think there is much interest.” So I did. And Senator Glenn by that time had become the Chairman of the Committee, and he said, “I always look back and I am grateful to Abe Ribicoff for giving me that suggestion.”

So I did put my name down. It was not my first choice. My first choice was the Environment Committee, which I was lucky enough to get on, but there was not much interest in this Committee. And so I also got put on it. The students probably have heard about the seniority rule in the Senate. This is the rule that basically says that you get the opportunity to move up in almost all cases based on how long you have been there. I remember that at the orientation session we had when we first arrived, there was a Senator named Wendell Ford from Kentucky, who had been a Senator for a long time. He came in and he said to the 10 or 11 of us who were new Senators, “A lot of the things you are going to find around here, you are not going to understand or they are actually going to annoy you.” He said, “That is the way I felt about the seniority rule when I got here. But, the longer I have been here, the more sense it makes.” [Laughter.]

So it goes. You never know how your seniority is going to play out because you never know what is going to happen to the people ahead of you in seniority on the Committee. I have been very fortunate to become the Chairman of this Committee.

In 2002–2003, this Committee generated the legislation that created the Department of Homeland Security, and when it came time to decide which Committee would oversee this new Department, they asked us to do that, in part because our Committee has had a really good reputation for bipartisan work, and I have had the



privilege to work with two Republican chairmen, Ranking Republicans when Democrats have been in the majority: Senator Fred Thompson, who left me to go back to "Law and Order"—I do not know how he could have made such a choice—and Senator Susan Collins from Maine. So the Committee is now known as the Senate Committee on Homeland Security and Governmental Affairs, but it is in the second capacity, Governmental Affairs, which is the oversight of how Federal programs are operating and how Federal money is being spent, that I am privileged to conduct this hearing today.

In a way, I want to use our State of Connecticut as a microcosm of the challenges facing all of our State and local governments as we try to get Federal stimulus money moving through our economy, protecting and creating jobs, and making investments in our future.

I am not going to spend much time talking about the economic problems that brought forth the stimulus because we live with them. This is an unprecedented economic experience.

Last year, the American people, American households, lost \$11 trillion of value, assets, and wealth in the loss of value in our homes and in the loss of value in stock markets and the savings and investments that we have had. In the State of Connecticut, since the recession began in December 2007 to January 2008, we have lost over 50,000 jobs. We had the worst month of job loss in Connecticut in February, the worst month in 15 years, in which we lost over 15,000 jobs.

It is that set of facts that led President Obama and his Administration, as they came into office, to reach out to Congress and to propose what we call a Federal stimulus package. The formal name of it is the American Recovery and Reinvestment Act. It is the largest Federal appropriation of its kind in American history, and it came about because the economic situation we are in is unprecedented. We have never had one like this.

This is not the Great Depression, thank God. Unemployment and the loss in the economy are nowhere near as great as they were then. And we have the beginning of some signs of hopefulness. The markets which measure all of this had their best month in years in March. There was the beginning of economic activity. Consumer spending went up a little bit. The newspapers today, here in the State, say that the Connecticut Business Industry Association did a survey of small businesses in the State, and it found that they were finding it easier in the month of March to get loans from banks, which has been a real problem.

But State and local governments are hurting, and will continue to hurt, and until we begin to create jobs again and stop the bleeding off of jobs with people becoming unemployed, we are not going to be anywhere near where we want to be. That is what occasioned the stimulus package, \$787 billion authorized over 2 years, and here is what the basic thought was.

There was a real problem in our economy: Subprime mortgages, loss of housing values, trouble in the financial sector and banking, people could not borrow money, the beginning of unemployment—real problems. Those real problems did two things: First, they created understandable anxiety, a lack of confidence in the American

people about their future economically, whether they were going to lose their jobs, for instance, or if they had lost wealth in the stock market or their housing values. And so people stopped spending, and spending drives about 70 percent of economic growth in our country.

A lot of economists told President Obama, and told Members of Congress, that there was a \$1 trillion gap between what the American people will normally spend and what will be spent. Businesses stopped investing because they could not borrow the money for this year and probably next year. And in that reality, the only entity, the only organization that could begin to spend to try to turn the economy around and restore people's confidence was and is the Federal Government. That is why the President made the recommendation to enact a stimulus, and why we adopted it. I was privileged to be in the middle of the negotiations to not only form the bill but to get the 60 votes we needed to get it out of the Senate to a conference committee and to pass and be signed by President Obama.

I believe that the stimulus package has begun to put money out into the economy in a way that is working, and I think that is part of why confidence has gone up and why some of the economic indicators have gone up. But there is a lot more that we have to do, and that is why we are really here this morning.

I will tell you that there were two goals that the Administration spoke of, and I think most Members of the Congress have, for the stimulus package. The first was to get money out into the economy to protect and create jobs. The second was to try to do it in a way that would make investments, significant investments in a better future for the American people; in other words, not only to stop the bleeding and build up the economy again, but to do it in a way that would be an investment in better quality of life and sustained economic growth, particularly in three areas—education, health care, and energy independence.

As you probably heard, under this program, the State Government of Connecticut is in some cases not holding all the money itself but in most cases distributing it, including through local governments, particularly education money. The State will receive \$2.9 billion in funding, and I am very glad we have been able to do that. This total does not account for other programs that will be funded under this that people will apply for directly from the Federal Government, nor does it count the payroll tax reductions that are beginning this month and will reduce the payroll tax for 1.4 million workers in Connecticut and their families, \$400 for a single worker and \$800 for a couple. Some people say that is not a lot of money. For a lot of people in our State right now, that is a lot of money, and it is going to enable them to maybe pay some bills off or maybe buy some things that they need that they otherwise would not be able to buy.

So, today, we are really focusing on that \$2.9 billion that is coming to the State Government of Connecticut for spending and also redistribution to other entities. And we are privileged to have with us a perfect group of witnesses, one representing the State, the others representing an education group, a health care group, and a

broadier group, which speaks particularly for children, but also for social services in our State.

So let me now go, with that introduction, to our witnesses. Each of them, I think we have told you, will have 10 minutes for an opening statement, and then we will go on to a question-and-answer period.

Our first witness is the Secretary of the Office of Policy and Management of the State of Connecticut, Hon. Robert Genuario. I cannot think of a better preparation for this job that he had than to be a State Senator. Since I was once one myself, I have a bias. Secretary Genuario, welcome, and we look forward to your testimony now.

**TESTIMONY OF HON. ROBERT L. GENUARIO,<sup>1</sup> SECRETARY,  
OFFICE OF POLICY AND MANAGEMENT, STATE OF CON-  
NECTICUT**

Mr. GENUARIO. Thank you, Senator Lieberman, and it is a pleasure to be here. Let me, on behalf of Governor M. Jodi Rell, extend my thanks to you for holding this hearing and giving us an opportunity to have a conversation, a dialogue about the stimulus package and its impact on Connecticut. We appreciate very much the effort and the rapidity with which this package was passed. It came to Connecticut when Connecticut, as other States, was going through a very difficult time.

I might add that the current economic crisis may adversely impact Connecticut to a greater degree than most other States because of Connecticut's dependence or involvement in financial services industries, both from the point of view of its population and from the point of view of the revenues that the industry generates for the State budget so that the State budget can provide services to many others.

So, by way of backdrop, at the time the Congress and the President were putting together the package for our Nation, Governor Rell, my office, and members of the Rell Administration, were putting together a proposed budget for the General Assembly's review, and we were facing very substantial deficits. Our revenue situation had deteriorated significantly. My office had projected a \$6 billion deficit back in January over the 2-year period. Since that point in time, my office has looked at the data that is coming in, and we are currently projecting a \$7.4 billion deficit.

So difficult decisions needed to be made, and the fact that the Federal Government was recognizing the problem that all States were facing and was providing assistance—not assistance to make all our problems go away, to be sure, but significant assistance by virtue of a variety of revenue streams targeted in many ways at those services that States historically have stepped up to the plate on and have provided for their populations.

So Connecticut, we believe, began even before the Federal legislation was adopted by including our best estimates of what that legislation would provide in Governor Rell's State budget. We have been working with various agencies at the Federal level ever since to make sure that we are in a position to maximize the benefits of

<sup>1</sup>The prepared statement of Mr. Genuario appears in the Appendix on page 252.

this legislation for Connecticut and Connecticut's citizens, and to do so in a way that makes Connecticut citizens proud and the Federal Government proud and keeps to the goals of transparency and accountability that are contemplated by the legislation.

To that end, Governor Rell issued Executive Order No. 25, which calls for the creation of a State accountability officer, a State transparency officer, and a stimulus project oversight officer. The governor is very focused on making sure that Connecticut leads the way in demonstrating how transparent a process this can be. Early on in the process, the governor called together groups of legislators, municipal leaders, representatives from the nonprofit community, and stakeholders of all sorts to try to put together a list of projects that would meet the shovel-ready definitions in the Federal legislation. That has been an open and transparent process. She created very early on in the process a State Web site to follow the workings of this group. Decisions that are made are posted immediately on the Web site as those decisions are made. Those meetings are public, recorded, quite transparent in the manner in which the decisions to move the stimulus money—particularly what I would call the shovel-ready or the infrastructure portion of the stimulus package money—out to Connecticut citizens and to the folks who will create the jobs and improve the infrastructure for the State of Connecticut contemplated by the Act.

As you might imagine—and I think as everybody recognized going forward—because of speed with which this legislation was developed, because it was developed at a time when States were putting together their own budgets, there has been and currently is a lot of interaction between our State agencies and their counterparts on the Federal level as policies on the Federal level are developed to tell us what we can do and what we cannot do with the money, how we can access it, what it is intended to do, what are the limitations, what are the condition on it.

Chairman LIEBERMAN. Are you finding the Federal Government personnel responsive?

Mr. GENUARIO. We are finding them to be very responsive, Senator, and that is really one of the most pleasant experiences about this. These are complicated questions. There is a clear policy contemplated by certain provisions of the Act, but by its nature, there is not time to adopt formal Federal regulations for the use of this money consistent with the speed with which we would like to see the money get out. But my office, and the offices of various State agencies, have had numerous phone calls, conference calls, meetings with their counterparts at the Federal level, and we have found the answers are coming very quickly and that the Federal Government is showing a demonstrable willingness to work with the States in order to solve problems that come up on a day-to-day basis. So we are very pleased with the Federal Government's response.

Chairman LIEBERMAN. Good.

Mr. GENUARIO. From where I sit, Senator, assisting the governor in promulgating and hopefully passing a State budget, the help that came to us by way of a stimulus package was very important to us. And as far as its impact on the State budget itself as a budget and as a mechanism to deliver services, those funds fall into sev-

eral categories. First and foremost, there is the increased Federal Medical Assistance Percentage (FMAP) Medicaid money, that Connecticut will share generously in. Connecticut will receive over the course of 3 years about \$1.3 billion additional Medicaid reimbursement. That will begin in fiscal year 2009, which is important because the State faces a significant deficit for the fiscal year that we are in. It will also assist us over the course biennium.

There are, appropriately, conditions although, in my view, not too onerous in terms of the use of that money. When the governor proposed her budget, some of those conditions were not known. We will necessarily withdraw a proposal or two that she had made that are inconsistent with those conditions. But, by and large, the additional FMAP money does not unduly constrain the States in our view in order to access it.

Perhaps I am speaking more from Connecticut's point of view. Connecticut tends to have relatively generous benefit packages, and I will use the unemployment compensation component as an example. Connecticut stands to get about \$87 million in additional unemployment compensation money.

I noted in some of the national colloquy that certain conditions are required; certain benefit levels at the State level need to be adopted in order to access that money. The truth of the matter is Connecticut already meets 95 percent of those conditions from a benefit point of view.

We did need—and the governor has proposed and the legislature is poised to adopt—one fairly inexpensive improvement to that benefit package in order to access that \$87 million. We are quite willing to do it. From where I sit, again, it will probably cost us \$2 to \$3 million per year. I think any businessperson would be willing to—

Chairman LIEBERMAN. That is a good deal.

Mr. GENUARIO [continuing]. Undertake that additional burden in order to access the \$87 million at a time when it is sorely needed.

The other significant component of the stimulus package that flows through the State budget is the State stabilization fund. Obviously, that is targeted primarily, though not exclusively, towards making sure that we are able to continue our commitment to funding public schools. And the governor has, in fact, proposed a budget that will provide an amount of money to public schools in Connecticut equal to that which it provided last year. The governor essentially flat-funded all of its major educational grants. And I say that with some pride because in this day and age of shrinking revenues, flat-funding is a sign of priority. We are not in a position to increase our funding in too many areas, so that if we are able to maintain our commitment over the course of the next 2 years and, therefore, be in a position to continue the gains in those areas in the out-years, it is a win for us.

I might add that Connecticut under Governor Rell's leadership provided one of the most significant increases in public school funding over the last biennium, so we are starting at a higher plateau than we would have been say 3 years ago.

The stabilization money does provide—and it is somewhat of a curious mechanism, but not one that I believe we will find difficult to work with. But we need to appropriate less than what we appro-

priated last year in order to access the money. But if we do so, then that money will then flow to the municipalities and the boards of education in amounts equal to what they would have gotten under the grant. It is not a provision that we think in the long run will provide us any difficulty. We will have to craft legislation that will accommodate that condition, but at the end of the day, the result will be the same, that every public education entity will get the same amount of money this year that it got last year consistent with the governor's proposal.

The stimulus package also provides additional money under Title IV-E in order to assist Connecticut in its efforts to provide programs and services for children who are in need of adoption and in need of the services of the Department of Children and Families, and we are grateful for that as well.

Beyond those three areas that flow through the State, Connecticut will receive approximately \$150 million—and when I say Connecticut now, I am talking about entities other than the State itself—in other education programs, primarily special education, which we are grateful for, and educational technology; \$450 million in transportation infrastructure money; \$48 million in clean water funding; \$64 million in weatherization; and \$38 million in other energy programs.

All in all, the stimulus package has provided the State with needed resources at a time when the State needs it the most. We are grateful for that, and we are particularly grateful with the efforts of the Federal Government to make clear the methods and conditions that we need to comply with in order to access these funds.

Chairman LIEBERMAN. Thanks, Secretary Genuario. That gets us off to exactly the right start, and I think your testimony perhaps shows—I tried to say this in my opening statement also—the main goal of the stimulus package was to get money out into the economy quickly to stop the slide down of our economy, but obviously also we had two other goals, which are: First, not to spend it so quickly that it is wasted or it is subject to fraudulent uses; and the second, obviously, is to make sure that it gets used for the purpose for which we intended it.

Let me ask you just a factual question at this point about the flow of money to the State now from the Federal Government. Has it begun in a significant way?

Mr. GENUARIO. We have not actually received the cash yet, but—

Chairman LIEBERMAN. But the check is in the mail.

Mr. GENUARIO. The check is in the mail. [Laughter.]

We do expect to be receiving it very shortly, particularly the fiscal year 2009 Medicaid money. Our counterparts down in the Federal Government have assured us that those dollars are available.

We need to file our applications. The applications are involved. I think we are poised to file our application for the energy funds today. I was told, though, late last night that the electronic components are not up to receive the application as yet. But those are things that will be worked out.

So, as you say, I think the check is in the mail. I am very confident that we will receive it by the close of business—

Chairman LIEBERMAN. In a timely fashion. I appreciate that. That is a good beginning.

The challenge here is to make sure that the money is spent for what we wanted it, not just to avoid waste and fraud but to get to the benefits we wanted. And I will admit that there were mixed feelings, at least, in the Congress, probably in the White House, too, about this. We do not want it to be used just to pay for the operations of State government that otherwise would have to be paid for in the State. On the other hand, clearly, if one of the things we are doing by getting the money to you is to enable the State and local governments, education, etc., not to have to let people go, then that is part of what we wanted to do. And that line is a difficult line, and I think it is one that we will probably hear about as we hear our next three witnesses.

John Yrchik is the Executive Director of the Connecticut Education Association (CEA), and education obviously was very much in the minds of Members of Congress and the President in adopting the stimulus package in all the ways that I have stated. So please proceed now with your testimony, Doctor.

**TESTIMONY OF JOHN P. YRCHIK, PH.D.,<sup>1</sup> EXECUTIVE  
DIRECTOR, CONNECTICUT EDUCATION ASSOCIATION**

Mr. YRCHIK. Good morning, Chairman Lieberman. I want to thank you for your invitation to appear at this hearing on the American Recovery and Reinvestment Act, and I would like to thank you, Senator Christopher Dodd, and other members of our congressional delegation for your roles in assuring the passage of this legislation. The CEA would like to commend you and other Members of Congress for recognizing the critical importance of education in our economic recovery.

In the next 2 years, over three-quarters of a billion dollars in new education aid will flow into Connecticut. This aid is unprecedented both in size and in nature. It is the very first time the Federal Government has stepped in to directly fund school funding formulas. But even with this enormous infusion of Federal dollars, like other States, Connecticut is projected to have layoffs and reductions in positions in a number of districts in our State. The reason for this, as Secretary Genuario has alluded to, is in part due to the enormous concentration of financial services jobs in our State. We have approximately 60 percent more financial services jobs than other States on a national average basis, and those jobs in turn produce many other jobs. So when the rest of the Nation has a cold, we catch the flu, and that is really what we are struggling with. The size of our deficit is a matter of great dispute in our State. One projection has it as high as \$8.7 billion, or approximately one-quarter the size of the entire budget.

Connecticut is one of the relatively small number of States that is proposing to use the State fiscal stabilization fund to supplant State aid that the State currently provides to municipalities. Our State may be alone in proposing to use the entirety of the State fiscal stabilization fund to backfill existing State education aid to municipalities with Federal dollars, and in doing this, our State will

<sup>1</sup> The prepared statement of Mr. Yrchik appears in the Appendix on page 256.

have reduced its actual commitment to education aid by over 14 percent over the next 2 years.

Connecticut's governor did have the option of using stabilization funds to exceed the fiscal year 2009 appropriation but chose not to do so. And as Secretary Genuario said, we are not funding municipal aid to education at the level of current services. And next year, the State will be contributing 21 percent less than what it would have contributed if it merely provided an increase sufficient to maintain current services at this year's level of education cost-sharing grants.

But, I have to say that as difficult as the situation is now, it would undoubtedly have been far, far worse had the American Recovery and Reinvestment Act not passed Congress. By way of illustration, our State Board of Education earlier this year passed a budget in which it cut education cost-sharing grants by 12 percent. Had a cut of this magnitude or anything like it survived the legislative process, it would have had catastrophic results on education in Connecticut.

Chairman LIEBERMAN. And I presume, if I can draw you out on that, that would have meant significant layoffs of teachers and other school personnel.

Mr. YRCHIK. Enormous. And so I think it has to be said that, as bad as things are now, they would have been considerably worse had these funds not been available, and that is a point that has to be stated categorically.

At the same time, because these are one-time funds and our State is using them to supplant existing State dollars, the question arises: What will we do when the funds run out and our State does need to begin, it seems, rather soon to develop a plan to deal with the hole in the budget that will come when the Federal dollars are no longer there? That is one challenge.

Another one is that as a condition of accepting the stabilization funds, the State has to make progress in four areas: Teacher effectiveness, standards and assessment, improving achievement in low-performing schools, and creating systems that track student progress.

In the governor's original budget, she eliminated the funding for a mentor program that would have been extremely important in improving effectiveness in our State, and particularly in ensuring teacher quality across Connecticut districts.

Chairman LIEBERMAN. Mentoring for teachers.

Mr. YRCHIK. That is correct.

Chairman LIEBERMAN. Not students, right?

Mr. YRCHIK. Yes.

Chairman LIEBERMAN. Important.

Mr. YRCHIK. In addition, her original budget eliminated funding for a program called CommPACT Schools, which takes some of our lowest-performing schools and, in a historic collaboration with the School of Education of the University of Connecticut (UConn), attempted to turn them around using a whole school reform approach that has been proven successful in many other parts of the country.

Both of these programs have been restored in the most recent budget of the General Assembly, and we are hopeful that they will survive the legislative process.



Last, with respect to transparency, we believe that our State's efforts to ensure transparency are adequate, and we believe that they are doing an admirable job in trying to track the use of funds. I would just say that we want to ensure that the need for transparency does not create so many administrative burdens that it becomes counterproductive, and that is something I think we will monitor as we go along.

On the subject of IDEA, our State will be receiving \$133 million in IDEA funds.

Chairman LIEBERMAN. Please define IDEA?

Mr. YRCHIK. IDEA is the Individual with Disabilities Education Act. The Federal Government originally committed to spend about 40 percent of the total costs of IDEA when the Act was first passed. Currently in our State, it spends something like 16 or 17 percent. With the stimulus package came an enormous infusion of new IDEA dollars. The State currently receives \$150 million in IDEA funds and over the next 2 years will receive an additional \$133 million.

Chairman LIEBERMAN. Almost doubling. Or a little less.

Mr. YRCHIK. A 60-percent increase in each of the next 2 years, correct. And one of the things that the last reauthorization allowed is for school districts to use 50 percent of the increase, just 50 percent of the increase, to supplant State and local funds currently being expended on special education to defray other costs in the school operating budgets.

In a time like this, when teachers are being laid off in many parts of the State, this would seem to be an important issue. But so far, school districts have not really moved to aggressively use the IDEA funds that can be freed up in this way to prevent layoffs. I think in part that is because at an initial meeting of superintendents, they were not told that they could. And then when guidance finally came from the State department, they were told that if they did, they could have holes in their operating budget 2 years from now.

But given that these funds are arriving in our States under the guise of an act whose primary purpose is to preserve jobs, to retain jobs, and to create jobs, it would seem to be important that we look at the potential uses of money in this way to do exactly that.

I would also like to talk about Title I, which is education for disadvantaged students. In fiscal year 2009, Connecticut received \$102 million and over the next 2 years will receive an additional \$97 million, roughly a 50-percent increase in each of the next 2 years. A perennial criticism of No Child Left Behind has been that it was underfunded, and one of the primary areas of criticism was that Title I was underfunded. And with this historic increase, it would seem we are much closer to our goal of properly funding No Child Left Behind.

The problem is that these are not ordinary times, and in the context that we are in, we are looking at effectively a reduction in State aid because level funding is a reduction for next year. We are looking at layoffs, eliminations of programs, positions, and pretty severe fiscal stress in many municipalities. And I think the question really is: Can \$97 million over 2 years adequately compensate

for the losses that will come to education from the distress that I have just mentioned?

In normal times, it would be used to provide professional development, to create after-school tutoring programs, pre-K programs, and other things that we know work. But at this time, it is difficult to know what its effect will ultimately be. It will ameliorate some of the effects of the distress, but whether it will ultimately be able to help districts fulfill the promise that comes with it is hard to stay at this point.

As with IDEA, we believe that a portion of these funds could be used at this time to help districts preserve their core education programs and bridge the shortage in revenues that they will experience between now and fiscal year 2011. What we need to do this, however, is clear guidance from our State department and from the Federal Government, and we need the ability to get this guidance on a rapid basis.

I would like to say just two quick points in conclusion: That the CEA stands ready to work with the State Department of Education in helping to ensure that these funds are used properly; our teachers at the local level stand ready to work with local school districts. And we believe that this is an important time for all of us to work together.

I would like to say, too, to reiterate what I said earlier, that the overall result of almost \$800 million in Federal funding is unreservedly positive. We believe that the promise of the Recovery Act is great, and on behalf of the CEA and the National Education Association (NEA), we very much appreciate your effort to hear our stories and to work with you toward economic recovery.

Thank you.

Chairman LIEBERMAN. Thank you, Dr. Yrchik, both for the tone and the substance of your statement. And I think you really highlight the moment we are at, a moment of real need in which this Federal money can avert and will avert some really disastrous consequences at the State level in education, for instance. But we want it to do more than that, and that is the challenge that everybody has here because we want it really to be not just a stop-gap now but an investment in a better future for our kids through the education system. It is not easy to do because there is a natural tendency to try to put your finger in the dike so it does not get blown away by the water. But, on the other hand, if I may continue this old metaphor, maybe we really need to rebuild the dike so that it is a better dike. That is the challenge, and I want to engage in some conversation after we get to the other witnesses about that.

Our next witness, speaking for the health sector, is Steve Frayne, who is the Senior Vice President for Health Policy at the Connecticut Hospital Association. He has been a long-time advocate and thoughtful spokesperson for better health care in the State. We welcome you now.

**TESTIMONY OF STEPHEN A. FRAYNE,<sup>1</sup> SENIOR VICE PRESIDENT, HEALTH POLICY, CONNECTICUT HOSPITAL ASSOCIATION**

Mr. FRAYNE. Thank you, Senator. Good morning. As you said, my name is Steve Frayne. I am the Senior Vice President for Health Policy at the Hospital Association, and we do appreciate this opportunity to testify on the benefits that the American Recovery and Reinvestment Act of 2009 will have for Connecticut hospitals and Connecticut communities. We also want to thank the hosts here for this wonderful facility and also for all of the students who are participating. I am sure some of them might feel a little anxious about some of the things we are talking about here, but I am sure you agree, as I am hopeful most of the panelists do as well, that really we do have the best and brightest folks working on these issues. I think we are all very confident that we will succeed, and succeed in a terrific way, in turning our economy around and producing some great things for the future.

I would certainly encourage all of them, as they are thinking about their future, to also consider careers in public service. These are terrific careers. They are very rewarding. Whether it is in health care, education, or in government, these are things that we would certainly encourage them to think about.

This morning, in terms of my testimony, I would like to talk about a few things. One is to give a little context about what hospitals are and who they serve. Second is to talk about how we are doing right now. And then third is to really talk about how the Recovery Act affords us some opportunities to, in fact, be able to advance where we need to go as both a hospital community and as a State as a whole.

Connecticut hospitals are really more than just facts and figures and dollars and cents. At their very core, hospitals are really people taking care of people. Each year, the more than 66,000 employees who work in Connecticut hospitals do their level best to provide the absolute highest quality of care that the citizens of our State need.

Last year alone, we had roughly 2 million days of care delivered by hospitals to patients in the State of Connecticut. We also had more than 4 million outpatient visits to the hospitals throughout the course of the State. Some of those visits, about a million and a half of them were emergency department visits; other visits, well over 600,000 of them, were for basic primary care services, basic physician services that individuals just could not find access to at a private physician's office, and they needed to seek out that care in a hospital.

We also contributed quite significantly to the overall economy of Connecticut. Last year, those 66,000 jobs together, with the direct employment and then the employment for all of the other jobs that actually provide services to hospitals, combined produced over 97,000 jobs in the State of Connecticut, almost \$13 billion in economic activity, and we purchased nearly \$6 billion in goods and services locally here in the State of Connecticut.

<sup>1</sup>The prepared statement of Mr. Frayne appears in the Appendix on page 267.

So, obviously, hospitals are a fairly significant part both of the economic health of the State as well as the personal health or contributing to the personal health of those who need our assistance when they are ill.

In the best of times, the ability of Connecticut's hospitals to contribute to the general economy as well as to providing high-quality care is often taxed, and taxed quite significantly. In a routine year—and, obviously, we are not in a routine year—it is quite typical for hospitals to experience well over half a billion dollars in losses providing services to individuals who are enrolled in State and Federal programs, as well as the uninsured. This is really a fairly significant burden, one which we have to figure out how to deal with on an annual basis. It never goes away and it grows larger and larger every year.

As I said, obviously these are not typical times, and what we are experiencing, unfortunately, for the very first time in our history is a situation where those instances where we have had investments that we were able to use to help offset some of those losses through Federal programs or State programs, those investments, not dissimilar to what other folks are experiencing in their 401(k)s or dollars that they might have had saving for the future, have declined quite dramatically over the last year. We are now in a situation where not only are they not contributing to our ability to manage some of these routine losses, they are actually adding to the losses on a routine basis. And this is really a very devastating situation that we find ourselves in at the moment.

Switching to hopefully some of the good news, thankfully, I think, Senator, with your leadership, Congress is delivering some very significant relief to the State of Connecticut. It is much needed, and we are clearly very appreciative of all the hard work that you and your staff and others in Congress have put forward to bring desperately needed funds into the State of Connecticut.

I am going to talk about four elements of the Recovery Act and how those might be particularly helpful to hospitals.

I think earlier, Mr. Genuario referenced the Medicaid match and how that will provide a significant benefit to the State, particularly in its ability to be able to continue to provide much needed access to health care. Where we stand at the moment in terms of how those funds are going to be used is we have kind of a range of options, anywhere from, on the upside or the best of situations as it currently looks, we may experience no cuts to our current levels of funding; and in the worst-case scenario, there are proposals out there where there may be potentially upwards of \$170 million worth of cuts over the course of the next 2 years.

This is a difficult situation, and I think it gets to the point that you were raising earlier, which is where is that fine line and do we find the right place where, on the one hand, we both stimulate the economy and preserve jobs and increase jobs in our State and, on the other hand, we also make it possible for the States to help balance their budgets. That is a very difficult line to find, and I think, respectfully, we all may have very different opinions sometimes around where that line may lie.

Our view, obviously, is that first and foremost those dollars are intended for Medicaid and need to be used for Medicaid. We think

that it is absolutely critical that we preserve access to health care for those folks who, through no fault of their own, find themselves in a situation where they need to rely on the State and Federal Government for their basic health insurance. So we certainly do not want to see any of those funds not used to both preserve access as well as to meet the growing number of individuals who need to use those services.

Chairman LIEBERMAN. So you would say your minimal goal for the use of the Medicaid reimbursement or support that is part of this bill, is that there be no cutbacks in services available to anyone in the State eligible for Medicaid?

Mr. FRAYNE. Correct. That is our minimum starting point for which we think those funds should be used.

Chairman LIEBERMAN. Let me just interrupt you. I do not usually interrupt, but since we are at home, Secretary Genuario, do you accept that goal or does the State accept the goal?

Mr. GENUARIO. We have proposed some changes to our Medicaid plan, changes that I think are reasonable. I do accept as a general premise that Medicaid is an important program, that there should be no deterioration in rates that we pay for services, and that there should be no deterioration in eligibility for Medicaid services. But I think the State should reserve the right and is entitled to reserve the right concerning the particular programs that it provides and whether or not modifications in those programs are warranted.

Chairman LIEBERMAN. So that means what?

Mr. GENUARIO. I will give you an example.

Chairman LIEBERMAN. Yes. Obviously, what I am interested in is whether it means a reduction in benefits under Medicaid in the State.

Mr. GENUARIO. I will give you a couple of examples, and they are examples that vary in range. But Connecticut, for example, for those who are dually eligible for Medicaid and Medicare, pays for preferred policies as opposed to benchmark policies offered under the Federal Medicare Part D plan.

Chairman LIEBERMAN. That is the prescription drug program.

Mr. GENUARIO. Yes. Under the governor's proposal, this year, given our economic times, we have suggested that the State will pay for benchmark plans but not for preferred plans. I know of no other State in the Nation that pays for the preferred plans.

So there are changes like that that I think are appropriate.

Chairman LIEBERMAN. Mr. Frayne, do you want to react to that? Would that meet your minimum threshold or does it go beneath it?

Mr. FRAYNE. I think in the example that the Secretary provides, it probably could meet it, but I think there are a number of other changes which have been proposed that, we have testified before the legislature that we think do not, for example, imposing co-pays on individuals, requiring them to share in a cost of the premium, I think changing who might be necessarily eligible for the program or some of the benefits of the program. I think in those instances we would hope, first and foremost, we use these dollars to make sure—we do not have to make it more difficult for folks.

Let me just say, we do genuinely appreciate this Administration and those in the legislature who are having to wrestle with these incredibly difficult problems.

Chairman LIEBERMAN. Yes, tough times.

Mr. FRAYNE. How to balance this and make it work. We certainly do not envy the decisions that they have to make. And I think it is our goal to, as respectfully as possible, communicate to them our views on how these things might work and how they could best be used and how actually they can help create jobs in the State.

One of the things that has been kind of a consistent theme of ours is that, in order for it to be a stimulus, it actually needs to have some portion of increased spending. If, in fact, all we do is crowd out the State dollar for a Federal dollar and there is no actual increase in spending, then, in fact, in part some of the stimulus impact has been lost.

We think, quite frankly, there is a way to balance the objectives of both preserving the Medicaid program intact for those who are in need of it, helping the providers so they can continue to provide that care, and having an enormous amount of funds left over to, in fact, contribute to the State budget. So we think we can meet all three goals.

Chairman LIEBERMAN. OK. That was an important exchange.

Incidentally, I would say this with regard to education, health, and the whole array of child services that Sharon Langer is going to talk about: Part of why I am doing a hearing like this and why we are continuing our oversight is, as I said earlier, to make sure that we are achieving in a difficult time the goals we want to achieve. And I will tell you that Congress will reserve the right to legislate again on this before this 2-year period is over if we think that the difficult balance—nobody is making it easy—between sustaining current services and investing in new services that are meant to improve our future, is not met adequately, not only here but across the country. I think you can expect Congress to get back in and mandate or speak more clearly in some areas of this law where, frankly, there was some room left for judgments at the local level.

So, I am sorry, go ahead, Mr. Frayne. Please finish your statement.

Mr. FRAYNE. There are a few other things that I would talk about that are in the Recovery Act. There is the provision to, in fact, provide to hospitals in particular access to additional funds to deal with the fact that the number of individuals in this State who find themselves without any access to health insurance at all and, therefore, perhaps not access to basic fundamental care. Those numbers of individuals are growing, and thankfully, as part of this legislation, there was a provision in there that said we are going to open up some additional funding to States to allow them to be able to pass that on to providers.

One of the caveats or one of the hooks that causes those funds to come in is at first the State has to be currently expending all of the available dollars that it could access. This is a program called the disproportionate share program. Every hospital in the State of Connecticut is, in fact, eligible for those, so it is not a program just limited to cities or towns. It helps suburban hospitals and urban hospitals and large hospitals and small hospitals.

Sadly, in this instance, as we see it, we are not going to be able to get access to those funds principally because, as it stands right

now, the State is not fully accessing existing dollars. So it would require in this environment to have the State actually increase spending, which is not likely—not possible, really. And, therefore, I think those dollars will not be able to be accessed for the purpose they were intended.

On this point—and I think the next two points that I am going to raise—as Congress thinks about these things in the future, one of the things that we would hope some thought is given to, particularly when the States find themselves in a very difficult place where they need to spend a dollar in order to bring in a dollar, perhaps it might be better in the future when the States find themselves in a situation where they literally cannot spend another dollar, even though they may want to do everything they can to help us, they just find themselves not in a position to do so. And I would at least propose for consideration that we find some way to make sure that those dollars that you are looking to send to us are not simply contingent upon the good will or the ability of the State to be able to access those funds.

Chairman LIEBERMAN. That is a good recommendation. Yes, I take your point.

Mr. FRAYNE. The last two things I would talk about are inter-related with each other. There are dollars that will flow through the Medicare program starting in 2011 over the course of 4 years. Actually, a fairly large sum of funds, probably about \$150 million, will come into the State of Connecticut over the course of 4 years. The purpose of those funds is to help hospitals, in fact, implement electronic health records so that we can actually improve the quality of care that we provide to patients. What many may not know is that these kinds of undertakings—electronic health records, physician order entry systems, and computerization, really of a lot of what we do in health care—are extremely expensive, very time-consuming, and could take multiple years to complete these projects. It would not be unusual for an average hospital to have to spend upwards of \$20 to \$30 million and be engaged in a 3 to 5-year project to implement these things. So these kinds of resources coming through us would be extremely beneficial and should go a long way to helping us succeed.

The very last point which is related to that is—and one I hope that we will be able, in fact, to work with the Secretary on and the balance of the Administration and the legislature—that there is another provision in the law which relates to this that says States can actually create loan programs to, in fact, help providers—not just hospitals but physicians and other providers—be able to borrow money so that they can, in fact, purchase these electronic health record systems, which we know are extremely expensive. And it is really unprecedented, I think, the benefit of this program, where the Federal Government will match \$5 to every \$1 the State is able to put forward.

Now, obviously, we realize it is a very difficult time for the State to even come up with the \$1, but we are hoping that, given the fact that this is not a grant but it is, in fact, a loan program, we will be able to find during the course of this legislative session both the will and the commitment and the means to be able to do this, because I think we really need to be looking out for the next several

years on how are we going to improve the care that Connecticut citizens want and expect.

So I think I would just conclude that, as I said earlier on, we are clearly very appreciative of all the hard work that you personally have put into this Act. And I think yourself as well as the Congress have really put before us really an unprecedented opportunity, one which we really just cannot afford to squander. We have to find a way to make this work. We have to find a way to balance both the needs of the citizens in Connecticut and the care that they need along with balancing the State budget. I am reasonably confident that we are going to be able to do that. Thank you.

Chairman LIEBERMAN. I appreciate that very much. Thank you.

I would just say a word to the students about something you said earlier, which maybe is not evident. The hospitals of Connecticut, the health care system, like the schools, do not just deliver a service, which is health care or education. They are tremendous centers of economic activity. In almost every city in this State, probably the largest employer or close to the largest employer is the local hospital. And part of why we want to keep them healthy is not just so that they keep us healthy, but that so they keep our metropolitan areas healthy economically. And part of why we want this money to be used to avoid the disastrous layoffs of teachers, for instance, that would have occurred without the stimulus funding is that, to say the obvious, you want to protect the jobs. I always feel the best thing government can do is to try to help people get and hold good jobs to provide for themselves. But if they lose their jobs, they obviously do not have the money to go out and buy the things they would normally buy, and that trickles down in the economy so that the recession gets worse and worse. Stores close, etc.; other people get laid off because the stores are closed.

Anyway, that is why at the center of this stimulus program the first goal was to protect and create jobs, for the jobs themselves but also for what they mean to the rest of the economy.

That is the end of my economic lesson for today, students.

Sharon Langer is the Senior Policy Fellow at Connecticut Voices for Children. Thank you for being here, and thanks for your patience.

**TESTIMONY OF SHARON D. LANGER,<sup>1</sup> SENIOR POLICY  
FELLOW, CONNECTICUT VOICES FOR CHILDREN**

Ms. LANGER. Thank you, Senator Lieberman. I am honored to be here today, and I echo many of the sentiments of the other panelists. I am here on behalf of Connecticut Voices for Children. For those of you who do not know, it is a research-based public education and advocacy organization which works statewide to promote the well-being of Connecticut's children, youth, and families. And I appreciate particularly the invitation to discuss the enormous challenges that our State faces in ensuring that the stimulus funds for health care and education are spent quickly, wisely, and fully.

And I echo Mr. Frayne's comment that I do not envy Secretary Genuario his job, but I want to say on behalf of those of us who

<sup>1</sup>The prepared statement of Ms. Langer appears in the Appendix on page 273.



are not part of the government, who are not either in the Executive Branch or the legislature, that we stand ready—and I think the Secretary knows that Connecticut Voices for Children stands ready—to be a partner, not merely to criticize, but to be a full partner in helping the State move through this very difficult next 2 or 3 years. And I am delighted that the Federal Government, represented by you, Senator, and Secretary Genuario today representing the State, that you are here together, that this is a dialogue that hopefully will continue on many levels.

I will just reiterate a couple of points that others have made.

We know that our State is reeling from the collapse of the financial markets, the slump in the housing market, and the alarming increase in our State unemployment rate, which I believe is approximately 7.4 percent. And at the same time, the governor and the State legislature are faced with tackling a projected State budget deficit, as we have heard earlier, of anywhere between \$6 and almost \$9 billion for the two State fiscal years that will begin July 1. And just to keep it in perspective—and I think maybe Dr. Yrchik actually said this—if we have a projected State deficit for 1 year that is anywhere between \$3 and \$4.5 billion of an \$18 billion State budget, that is approximately 25 percent of our State budget, which is unprecedented. And at the same time, Connecticut, our little State, which has 169 cities and towns, faces terrible budget choices, including the town of West Hartford that I live in. And as a result, I agree that the Federal stimulus dollars have come none too soon to help our State keep its commitment to children, struggling families, and all the residents of our State.

I also want to reiterate what has been said before about the Federal Government agencies—the Department of Health and Human Services, the U.S. Department of Education—it is seemingly unprecedented that they have been able to issue guidances to help the States understand and interpret the stimulus legislation. And I think that those kinds of efforts by the Federal Government are enormously helpful. It is my understanding that the Federal Government and its State partners are on the phone, practically daily and for weekly conference calls.

I would urge both the Federal Government and the State government, to engage nongovernmental stakeholders in these conversations. I was in Washington recently, and one of the general counsels for the Department of Health and Human Services talked about the fact that they are trying to figure out how to reach out to others who are very interested in understanding how this money is used, both to make sure that it fulfills the multiple objectives to stimulate the economy and to preserve critical services. It is also so important that everyone knows what is happening on the ground so there is not unnecessary concerns about waste or fraud. I mean, everyone has to be vigilant given how much money is at stake and how quickly the attempts are being made to move it on the ground.

We were particularly pleased that the Department of Health and Human Services, its Centers for Medicaid and Medicare Services, came out with a guidance that really explained to the States what they can and cannot do in order to receive the increase in the Federal Medicaid matching funds. And I just want to say, for those of

you who do not know, that the Medicaid program in Connecticut alone provides critically needed health care services to one out of four children. Over 30 percent of the births in this State are to moms on our Medicaid program (which includes those moms on the Healthcare for Uninsured Kids and Youth (HUSKY) A program).

While the guidance from the Federal Government and the law make clear that the States cannot cut back their eligibility rules, there are many other ways, as we know from years and years of research, that you can create either intended or unintended barriers to getting families on publicly financed health programs, keeping them on, and getting them services. Proposals that have been put forward to institute cost-shifting onto low-income families, persons with disabilities, or elderly folks, garner savings by inhibiting people's ability to either get on the program or to access the health services. So we encourage both the Federal Government and the State Government to really carefully assess whether such proposals are in the best interests of children and families.

I would also point out that we have to appropriate the Medicaid dollars, in order to draw down the stimulus funds to appropriate the money. We have to spend the money in order to receive Federal reimbursement. And so there is not a guarantee. And so to the extent that we are cutting back in our Medicaid budget, for example, we put at risk our ability to access all of the Federal dollars that we get from the Federal Government.

I also want to reiterate what Mr. Frayne said, that we are worried that Connecticut may forego opportunities to utilize all the Federal funds available because Connecticut, quite frankly, has a long history of leaving Federal funds on the table, whether those are Medicaid funds, as Mr. Frayne said, a disproportionate share of hospital payments. During the 10 years of the Children's Health Insurance Program, we left a lot of money. Delightedly, the law with your help and the help of your colleagues, Senator Lieberman, the Children's Health Insurance Program (CHIP), was recently reauthorized. It is a fabulous law. It attempts to fix the funding problems to give States many options to cover more children, to simplify eligibility requirements and processes, to do outreach. And, quite frankly, Connecticut is very unlikely to take advantage of most of the opportunities in that law, partly because of our fiscal crisis and partly because Connecticut in some ways has been ahead of many other States, and it will just be a very difficult process.

The other challenge has to do with the way that Connecticut actually budgets. I do not know if there are other States that do this, but we are one of a few States that gross budgets both the Federal Medicaid dollars and actually the Title IV-E dollars, which, as Secretary Genuario said, goes to fund our child welfare program to help families adopt children. Those are really our poorest children in the State. And we also gross budget, which means we appropriate many of the Federal block grant funds that the Federal Government sends us.

So what that means in plain English is that the Federal and State dollars are combined in line items of the State budget. For example, the anticipated Medicaid stimulus funds in the form of the increased what they call Federal Medical Assistance Percentages (FMAP) payments to the State will just appear as a Medicaid

line item in the State Department of Social Services budget. And as a result of this longstanding practice of including the Federal funds without explanation in the State budget, it will be difficult to track the actual use of the stimulus funds.

I am delighted to hear from Secretary Genuario, and after I wrote my testimony, I did become aware that the governor has issued an executive order to create various positions, a stimulus project oversight officer, and the like. And so, in order to facilitate increased transparency and accountability, we would urge the governor to make sure that any work of these officers is put on the State recovery Web site and that the work of any work groups that Secretary Genuario referred to is also on the State's recovery Web site.

I would also let you know that Connecticut Voices for Children has created our own web page concerning the Federal stimulus, and so as soon as we see something new, whether it is a guidance from the Federal Government, information from Secretary Genuario's office, or elsewhere related to the implementation of the stimulus, we have put that information on—

Chairman LIEBERMAN. Ms. Langer, let me interrupt and I apologize. The time is going on.

Ms. LANGER. I am basically done.

Chairman LIEBERMAN. Let me say for the record that we are going to enter everybody's statement in the record in full—and I have read them; you have some good statements. I want to leave some time for back and forth. But I appreciate what you have said.

I actually want to pick up on the final point that you made. The Recovery Act itself and the President are very set on this being as transparent and accountable a program as we have ever had in the Federal Government, particularly using technology and the Internet. The government set up a Web site called Recovery.gov, and as of last Thursday, when I held my second hearing on this in Washington, the Web site had received over 300 million hits since about the middle of February when the Act was signed. It is quite startling how much interest there is in what is happening, and the President has set some very high standards that have never been met before here for people to be able to follow contracts, and to follow money from the Federal to the State to the local level.

So I want to ask you, Secretary Genuario, first, what the State is doing to try to comply with those requirements?

Mr. GENUARIO. The State has its own Web site.

Chairman LIEBERMAN. Specifically with regard to the stimulus?

Mr. GENUARIO. Absolutely.

Chairman LIEBERMAN. What is that address? Ah, I got you.

Mr. GENUARIO. You got me on that one. It has its own Web site. I think it is up on the governor's—

Chairman LIEBERMAN. Ms. Langer, what is it?

Ms. LANGER. I have it.

Mr. GENUARIO. Terrific.

Chairman LIEBERMAN. What is it?

Ms. LANGER. It is [www.recovery.ct.gov](http://www.recovery.ct.gov).

Chairman LIEBERMAN. That is [recovery.ct.gov](http://recovery.ct.gov), good.

Mr. GENUARIO. Thank you.

Ms. LANGER. You are welcome.

Mr. GENUARIO. I was going to point out before that when I want information, I go on Connecticut Voices' Web site. [Laughter.]

But Governor Rell's office, early on, formulated its own Connecticut stimulus Web site. It can be accessed directly. It can be accessed off the governor's own Web site. The minutes of every working group meeting are posted on that Web site. Decisions that the working group make or that the governor makes following recommendations of the working group are posted on the Web site. Decisions have already been made with regard to certain Department of Transportation infrastructure. Not only have those decisions been made, but as contracts are entered into, those will be posted on the Web site.

So I think Governor Rell has actually been in the forefront of making sure that this is a transparent process. Backing up, even before that, she engaged a variety of stakeholders in order to help make decisions in these areas.

Chairman LIEBERMAN. That is really important, and to say what is obvious to you at the table, this transparency that you will find on the Federal Web site and now on the State Web site is important for many reasons, one of which is obviously for people to figure out how to access funding under the stimulus bill; but the second, of course, is to see how it is being spent and in a certain sense to enable any citizen to become a whistleblower, to say, for example, the Web site says that this money is being used to build a new building in my town, and I live across the street from that property and nothing is happening. So it is very important.

As part of this desire to make sure the money is spent wisely, we set up a Recovery Accountability and Transparency Board, which is being headed by Mr. Devaney, who is the Inspector General at the Interior Department. He has said that one of his goals will be to try to help the States in fraud prevention and waste prevention by conducting briefings.

Is that something you think would be helpful for State officials?

Mr. GENUARIO. I do think it would be helpful, and I think we all need to be conscious of the fact that this is a lot of money going out the door relatively quickly.

Chairman LIEBERMAN. Right.

Mr. GENUARIO. So I think that would be very helpful.

Chairman LIEBERMAN. Incidentally, we appropriated, believe it or not, \$250 million over the 2 years for the hiring of additional inspectors and investigators for the inspectors general to pursue the spending of money across the country, just as a kind of guarantee.

I know you mentioned some appointments Governor Rell has made. Governor Schwarzenegger recently got some attention by employing a separate inspector general at the State level to monitor stimulus spending in California. Is the governor contemplating anything like that?

Mr. GENUARIO. She has made several appointments. She has appointed a transparency officer, an accountability officer. We are looking to hire a stimulus officer who will track each and every project within that office.

Chairman LIEBERMAN. So that would be the equivalent of what Schwarzenegger has done in California.

Mr. GENUARIO. Exactly.

Chairman LIEBERMAN. And I think in your prepared testimony, Ms. Langer, you endorsed a State Senate bill?

Ms. LANGER. Right, and it was a Senate bill before the State legislature that basically would set up a commission to do what I believe Secretary Genuario is talking about. We applaud the governor for instituting these kinds of offices, and what is important to us is the transparency and the opportunity to give feedback.

Chairman LIEBERMAN. So do you still favor the creation of a State commission on Federal stimulus fund distribution, or do you think what the governor has done satisfies that?

Ms. LANGER. All I know about what the governor has done was in the press release, so it appears to do that. I guess the question is whether the commission goes farther because it is made up of a group of people rather than just several individuals.

Chairman LIEBERMAN. Secretary, does the governor have a position on this bill? Are you familiar with it?

Mr. GENUARIO. I am generally familiar with it, and I think the governor's position is that the Federal legislation sets up the Executive Branch as the director of most of these funds, though not all. And to the extent that the Federal legislation sets that up, that ought to be the system that Connecticut uses.

With regard to advisory commissions or advisory boards, the governor has frequently worked with the legislature in terms of creating those types of bodies, and I doubt whether there would be an objection to that.

Chairman LIEBERMAN. Let me ask you about some of the questions Mr. Frayne raised about the State losing the possibility of Federal funding because of its unwillingness or inability to put in the State's share. Would you respond to that?

Mr. GENUARIO. Well, over the course of the last several years, the State has, I think, gone to great lengths to maximize, to the extent possible, Federal reimbursement. Now, I believe he is correct that there is some room within our Disproportionate Share Hospital (DSH) pools for additional State appropriations that would result in additional Federal reimbursement, though if memory serves me, the DSH pools are not eligible for the increased FMAP stimulus reimbursement.

Chairman LIEBERMAN. I believe that is right.

Mr. GENUARIO. So there would not be any increased Federal reimbursement.

There are times when, pursuant to the amount of revenue we have available, we spend what we think is reasonable and obtain the Federal reimbursement that is appropriate. You cannot always spend a dollar to chase 50 cents, and there are probably times where hospitals and other providers would like to see us increase rates in order to get additional Federal reimbursement. And to be sure, we have done what we think is reasonable.

I will point out that over the course of the last 2 years, Connecticut has increased Medicaid rates substantially—clearly not to the extent that some of the providers in the hospitals would like. But there has been a substantial movement towards increased Medicaid rates over the course of the last 2 years, and those increased rates will remain in effect under the governor's budget, and

presumably under the budget that finally passes, we will get the additional FMAP for those increased rates, though not for any DSH payments.

Chairman LIEBERMAN. Let me ask you a question that each of the other three witnesses in one way or another raised. And I know it is hard, particularly when you are in the midst of the budget crisis the State is in, to look too far forward. But I guess some people call it keeping away from the edge of the cliff. In other words—and Dr. Yrchik I think stated it very explicitly—the significant additional Federal funding for education that will flow through the States to the local governments for education purpose will go on for 2 years. Those funds are stopping some significant cutbacks that otherwise would have occurred. In one sense certainly with IDEA and with Title I of No Child Left Behind, they are helping to meet commitments that the Federal Government has not met, where the Federal Government set a mandate but did not fund it.

But then what happens after the 2 years? In other words, obviously we all hope and I believe that the economy will be doing better so that tax revenues will be coming in at a more normal pace 2 years from now for the State and local governments; but, nonetheless, we have a real challenge ahead.

Mr. GENUARIO. Well, I thank Dr. Yrchik for raising it, and thank you for asking the question, Senator, it is not something that we find hard to look at. It is something that we look at very carefully. And in fiscal year 2012, we will have some significant issues.

I might add that not only will the stimulus money go away, but under anybody's budget—let me back up just very briefly.

One of the things Connecticut has done right over the last 4 or 5 years, it has been very diligent in building up its budget reserve fund. And, clearly, that budget reserve fund under anybody's proposal will be utilized over the course of the next 2 years. So that when we get to 2012, we not only will have, presumably, a loss of stimulus money, as is intended, but we will no longer be able to rely on our budget reserve fund. So 2012 will be a very challenging year. I estimate that our structural deficit for 2012, if all goes well, will be in the area of \$1 billion plus.

So we have 3 or 4 years of difficult budget cycles ahead of us, and one of the reasons we make decisions that we make in terms of not expanding programs in 2010 and 2011 is because we know there is a problem in 2012 and we need to be conscious of that as well.

Chairman LIEBERMAN. Let me ask a specific question about Head Start funding. The stimulus bill included \$2.1 billion for Head Start funding. Last week, as I understand it, a small portion of those funds were released basically for cost-of-living increases and quality improvement for existing grantees. And, of course, I hope the Department of Health and Human Resources moves quickly to provide information on how you can apply for the bulk of the remaining funds.

But I want to ask you, Secretary, how do you envision, the State best utilizing the Head Start funds to improve early support and education services? And I will ask Ms. Langer and Dr. Yrchik whether they want to comment.

Mr. GENUARIO. Well, early childhood education has been a significant goal of Governor Rell since she has been in office, and we have had a fairly significant expansion of those services over the course of the last several years, including Head Start but also including some State-funded programs.

We think that we have built up an infrastructure for early childhood education that will serve us well and be able to better access some of the Federal dollars for Head Start than we might otherwise have been able to do. But it is money that will flow through Connecticut's Department of Social Services (DSS), will move to appropriate grantees as expeditiously as possible. A number of the Head Start programs are run through the Community Action Program (CAP) agencies in the State of Connecticut. They will continue to be, by and large, the providers of the services for those programs, and that money will flow through DSS to those providers consistent with that legislation.

Chairman LIEBERMAN. Ms. Langer, Dr. Yrchik, do you have a response to that and how you would hope this money would be spent?

Ms. LANGER. Well, we have made progress, but it is like a lot of areas where we need to do more. And I actually would like to defer the answer. There is someone in my office, another senior policy fellow, who really knows far better than I do about the details of this area.

Chairman LIEBERMAN. That is fine. We will leave the record open for filing of that kind of statement.

Dr. Yrchik, do you want to add anything?

Mr. YRCHIK. I would like to make a comment about early childhood in our State. I think that several years ago we really began to make considerable progress in this area. We agreed that relatively soon teachers of early childhood would have to be certified or have a B.A. in early childhood development. It was landmark legislation. The governor created a policy council to advise her on expanding early childhood opportunities. But a combination of things has occurred this year which I think has probably set us back.

The governor disbanded her Early Childhood Policy and Research Council. The economic circumstances of our State have caused the number of slots for early childhood to be level funded. And our progress has been, I think one would have to say, halted. So I think everyone in the State recognizes that this is a critical area and will be an enormously important area for improving student achievement over the long term.

At the same time, the funds that have come into the State through the stabilization fund, IDEA, Title I, those that could have been used to buttress support for early childhood programs have largely been used for other purposes or certainly have not lived up to the potential that they would have had in ordinary times.

So I would say that I think while our State recognizes the importance of this area, we really have been dealt a blow by the economy, and there is no getting around that fact.

Chairman LIEBERMAN. Yes, I agree. That is the corner we have to turn.

Let me ask a last question to you, Mr. Frayne. This bill has a lot of traditional infrastructure investment in it, which has been

proven to create jobs, protect jobs, and the money flows to highways, bridges—significant investments I am really pleased to say, in mass transit. But one of the more interesting new infrastructure investments the bill makes is \$2 billion in health-related information technology. This is a sort of transition to the next great challenge we are going to face in Washington this spring, early summer, which is to really get into health care reform, both to provide affordable health care for every American and also, obviously, to try to reduce the costs of high-quality health care.

Just give us a little bit of a sense of the hurdles we need to get over so that Connecticut receives all the health information technology funding to which it may be entitled. And give us an idea of how this money will be spent by some of the hospitals here in the State.

Mr. FRAYNE. Sure. Thank you. As you noted, one of the things hospitals have been working on for quite some period of time is to evolve their plans to go from a paper-based world into what we would call an electronic world, a computer-based world, where all of the information would be able to be transferred by computers. And there are enormous benefits to doing that. One, it would hopefully make us much more efficient than we are today in the care that we deliver, and probably an even more promising advantage of doing that is not only that we will become more efficient and actually help the economy as our cost structures will hopefully come down slightly over time, but also it will actually help improve the quality of care that we deliver to folks by having access to what were their most recent tests, what were the results of those tests, did they have an x-ray over at another facility, and what did that look like so we can get that without having to duplicate that test. So these are kinds of efficiencies and economies and quality improvements which are really desperately needed.

The good news is that nearly all of the institutions in this State are on that journey already. They are making significant investments in personnel, in time, in energy, and in dollars to evolve, in fact, from where we were to where we need to go.

The current challenge that we are facing is not dissimilar to, really, many other industries in that the markets to borrow money from are essentially closed. We cannot go and issue bonds, for example, through our State bonding authority. If we had the ability to do that, the interest rate currently would be too high. And the typical vehicle that we would use—and this is a little inside ballpark, but if you would bear with me one second—bond insurers—these are entities that actually improve the creditworthiness of our bonds—they have not fared very well recently in the economy. Actually, the underlying creditworthiness of hospitals now happens to be higher in some instances than the entities we rely on to help boost our creditworthiness. So it is an unfortunate turn of events.

But the combination of all those things essentially means you cannot get the money to borrow to be able to implement these projects, which everybody knows to an absolute certainty are critical for our future. And, one of the things that we are very hopeful of that we will be able to do over the course of the next few months, even in a very difficult State budget, is to be able to work with the State and your offices and other members of our congress-



sional delegation to put in the application to create this loan program, because thankfully in this instance now the Federal Government is saying, "We think this is an important goal, we want you to get there, providers, and we are going to help you get there by allowing you to borrow the money from us."

So I think if, in fact, we can work with the Administration and those in the legislature to make that happen, it would be really terrific.

Chairman LIEBERMAN. I would look forward to helping in any way I can.

I want to thank the four of you. Your testimony has been very helpful to me. Congress and the President's initiative did something that we have never done before, certainly not at this dimension, in passing this stimulus program. That is because we are facing an economic challenge the likes of which we have never faced before. We worked hard to get our fair share of it, Senator Dodd and I and all the members of the congressional delegation from Connecticut, for Connecticut. So it is very important to us, of course, that it be used well and effectively to protect and create jobs, to move more money through the State economy, and hopefully to make some investments in a better future.

I acknowledge the natural tendency to use the money to survive. We are going to constantly push to do more than that to try to use it in a way that is an investment in a better economic future and a better quality of life for people in the State. My own impression from the testimony that you have given, all four of you, is that we are off to a good start here in Connecticut. But I want to stay involved with you and others here. I know there are others who were good enough to come to the hearing. I saw some firefighters and police officers; they benefit from other programs that are part of the stimulus. Very important. There are other recipients who are here. Not only do we have a Web site in my office, but I invite you to call me or call our office, either here in Hartford or in Washington, with any ideas you have or anything you want to report to us about how this money is being spent, because it is your money. That is the bottom line, and we want to make sure that you benefit from it. So I thank you for that.

In the normal course, the record of this hearing—and we are keeping a transcript of all of this—will be open for 15 days if any of you want to submit additional statements. In the normal course, other Members of the Committee may submit questions. I doubt that they will ask you questions. We may have one or two follow-up questions. And then I would say to anybody else, and this is a little bit unusual, but if anybody else in the audience wants to file a statement with the Committee, please do so and it will be printed in the official record of this hearing.

I cannot thank you enough, those of you who testified, those of you who were here. This is probably the most attentive, well-behaved group of students that I have ever had sit at a hearing.

[Laughter and applause.]

There must be some future Senators up there, maybe even Presidents. Anyway, I thank you all, and with that the hearing is adjourned. [Applause.]

[Whereupon, at 11:48 a.m., the Committee was adjourned.]



## **FOLLOW THE MONEY: STATE AND LOCAL OVERSIGHT OF STIMULUS FUNDING**

**THURSDAY, APRIL 23, 2009**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 9 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, Carper, McCaskill, Tester, Burris, Bennett, Collins, and McCain.

### **OPENING STATEMENT OF CHAIRMAN LIEBERMAN**

Chairman LIEBERMAN. Good morning, and welcome to this fourth in a continuing series of hearings that our Committee is holding on the American Recovery and Reinvestment Act to monitor how effectively and efficiently the \$787 billion in tax cuts and spending are being used, but also to make sure, to the extent that we can, that it is doing the job that we, in Congress, intended it to do, which is to breathe life back into our economy.

While the Office of Management and Budget (OMB) tells us that \$60 billion of the Recovery Act money has been committed so far, the vast bulk of the Recovery Act money is still in the pipeline. One of the questions that I want to ask the witnesses today is whether they feel the Federal Government is moving this money out into the economy as rapidly as it could, because, obviously, that was the goal that Congress had, with an understanding, as one of the witnesses—I think, Mr. Scheppach said—“you have got attention here. You want to move it out as quickly as you can, but you want to make sure it is spent efficiently and not wastefully.”

Personally, I am impressed by the extensive planning, at all levels of government, to meet the Act’s accountability and transparency provisions, which obviously are critical to creating pressure for effective, efficient, and non-wasteful spending of the money. I am also impressed by what appears to be a strong spirit of cooperation between Federal, State, and local governments in implementing this Act.

But the next few months are going to be the real test as to whether we can ramp up spending quickly enough to stimulate the economy the way it needs to be stimulated and the way Congress intended with this American Recovery Act to have it stimulated. And to do that, we are asking all levels of government to do more, to do it well, and to do it in record time.

On April 7, I convened a field hearing for our Committee in Connecticut. And the State Secretary of Policy and Management, the chief budget officer, if you will, in Connecticut, testified that the Federal Government has reacted swiftly to his questions on behalf of the State and, he thought thus far, has imposed an acceptable level of red tape, or at least kept it to a minimum.

However, during that hearing, he also testified that there were very important implementation challenges from a State level; in particular, the need to give State and local governments clear direction and whether some of the Recovery Act money can be used to help pay for administrative and oversight costs. And I hope that the witnesses will talk about that today.

We know that the Act includes \$250 million for additional Federal investigators and inspectors to be hired to monitor from the Federal level, but about \$300 billion, by the last calculation we saw of this, in stimulus spending will be under the supervision of State and local governments. And, of course, those State and local governments are themselves under real fiscal financial pressure now. And the question is whether they have adequate personnel to monitor the spending at the State and local level. Therefore, I know they have asked for permission to use Federal stimulus money to retain personnel for that purpose.

I am very pleased that this morning, Vice President Joe Biden has released a letter to Senator Collins and me,<sup>1</sup> indicating that his office is working on this, and that OMB will be issuing guidance soon that will give new flexibilities to the States and local governments to cover administrative costs with the Recovery Act funds. In this balance that we are trying to strike, it seems to me that makes a lot of sense.

In the interest of moving ahead with the hearing, I am going to put the rest of my statement in the record.<sup>2</sup>

I do want to say how pleased I am that the Acting Comptroller General, Mr. Dodaro, is today going to release before this Committee his first bi-monthly report on State and local spending under the Stimulus Act as required by the Act.<sup>3</sup> The Government Accountability Office (GAO) helps us enormously in performing our function of oversight on this critical piece of legislation.

It is too early to say. There are obviously some glimmerings of hope about some movement in the right direction in the economy. We are not going to know until more of the stimulus spending is actually out there. And, of course, more significantly, beyond the jurisdiction of this particular Act or the purview of this Act, until all the steps that the Treasury Department, the Federal Reserve, and other institutions are taking to try to reestablish the health of the financial sector of our economy, and to get money flowing again, from banks, to businesses and individuals. Until all that happens, we are not going to have the kind of recovery, or the kind of confidence, that will lead to the recovery, that we need.

But anyway, we are pleased to have the three of you here: Gene Dodaro, and then a front-line report from Ray Scheppach of the

<sup>1</sup> The letter referenced by Senator Lieberman appears in the Appendix on page 283.

<sup>2</sup> The prepared statement of Senator Lieberman appears in the Appendix on page 277.

<sup>3</sup> The GAO report referenced by Senator Lieberman appears in the Appendix on page 350.

National Governors Association, and Carolyn Coleman of the National League of Cities. We look forward to your testimony today. Senator Collins.

#### **OPENING STATEMENT OF SENATOR COLLINS**

Senator COLLINS. Thank you, Mr. Chairman.

The American Recovery and Reinvestment Act is vital legislation intended to boost our troubled economy and to create and save jobs. If properly implemented and overseen, the law will also improve our Nation's roads and bridges, prevent cuts in health care, and provide important investments in education and science, while helping to turn our economy around.

State and local governments are playing a critical role in distributing, spending, and measuring the impact of Recovery Act funds. The GAO estimates that State and local programs will receive about \$280 billion under the law. As a result, they must prepare to handle the challenge of managing and overseeing this influx of new funds, a resource-intensive undertaking.

This challenge is further compounded by the fact that many State and local governments are facing major budget shortfalls that often leave them short-staffed. Like the Chairman, I, too, welcome the Vice President's letter this morning, which tells us that new flexibility is going to be allowed for States to recover the costs of certain administrative activities.

It would indeed be unfortunate and ironic if money is lost to waste, fraud, and abuse because States had insufficient funds to hire the necessary contracting officials, auditors, and oversight employees to ensure that the funds are well spent.

The Recovery Act also creates several important oversight mechanisms that the Chairman and I worked hard to ensure were included. These oversight mechanisms include the bi-monthly reports from the GAO on the use of funds by selected States and localities. The GAO is issuing its first of these reports today, and we are eager to hear the progress that State and local governments have made in developing plans and internal controls to ensure that the Recovery Act funds are not lost to waste, fraud, and mismanagement.

Today's hearing will also explore the mandates for accountability and transparency placed on State and local governments under the Recovery Act, as well as how quickly the money is being spent. This was a major issue in the Senate debate. The Senate was determined to make sure that the final version of the bill had a quicker impact on the economy by having a faster spend-out rate than the House bill had.

I am pleased to welcome, not only the GAO, but the National Governors Association and the National League of Cities to this hearing. These associations can provide useful insight into the innovative approaches State and local governments are taking, including how they are planning to communicate funding opportunities to hospitals, fire departments, businesses, schools, and non-profit organizations. A complaint that I hear from my State, is that a lot of the intended beneficiaries of this funding are still uncertain how to access it.

In addition, I want to hear about the steps that States are taking to ensure that the infrastructure contracts are awarded competitively, fairly, and effectively, and, of course, to ensure that taxpayer dollars are not wasted.

Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Collins.

I welcome Senator McCain and Senator Bennet.

And now we will go right to Acting Comptroller General Dodaro.

Thanks for being here and thanks for issuing this first report before our Committee this morning.

**STATEMENT OF GENE L. DODARO,<sup>1</sup> ACTING COMPTROLLER  
GENERAL, U.S. GOVERNMENT ACCOUNTABILITY OFFICE**

Mr. DODARO. Thank you, Mr. Chairman. Good morning to you, Senator Collins, Senator McCain, and Senator Bennet. We appreciate the opportunity to be here today to discuss the results of our first bi-monthly review of the use of the funds by selected States and localities.

As I mentioned to this Committee on March 5, when we were here to outline our plans, our review focused on 16 States and the District of Columbia across the Nation that will account for about two-thirds of the total amount of money that is allocated by the Federal Government to States and localities. And I also mentioned that we were going to follow these 16 States and the District over the next 2 or 3 years to do a longitudinal study of how they use the money but also what the impact of the Act had been and whether or not it was going to achieve its objectives.

This first chart explains why a longitudinal study is important.<sup>2</sup>

This is the estimated Federal outlays by the Congressional Budget Office (CBO) and other information we have put together as to when the Federal moneys will be outlaid to the States and localities. And as you can see, there is a ramp-up here in Fiscal Year 2009, but a lot of the outlays will be in 2010 and 2011 and in ensuing years.

Now, as the next chart will show,<sup>3</sup> for this fiscal year, Fiscal Year 2009, there will be about \$49 billion outlaid to the States and localities. Most of that, 90 percent of that, will be in the health area, education, and transportation.

Now, over time, as you can see, this chart compares Fiscal Year 2009 to 2012. The composition of the Federal spending will change. While a large part, 64 percent, this fiscal year will be spent in health care, as represented by the red piece of the pie, by 2012, that will be only about 1 percent. That is because the increased Federal share of the Medicaid program is for a 27-month period that will stop at the end of 2010.

You can also see that the amount of money that is going into community development, energy, and environment, will increase along with the transportation spending as new programs come on line, the broadband program, high speed rail program, and some of the housing and community development initiatives.

<sup>1</sup> The prepared statement of Mr. Dodaro appears in the Appendix on page 286.

<sup>2</sup> The chart referenced by Mr. Dodaro appears in the Appendix on page 326.

<sup>3</sup> The chart referenced by Mr. Dodaro appears in the Appendix on page 327.

Our first bi-monthly review, therefore, focused on the three programs where there is the largest amount of money to be spent during Fiscal Year 2009: The Medicaid program, the highway program, and the State Fiscal Stabilization Fund. Now, in the Medicaid program, the 16 States and the District that we looked at received an allocation from the Centers for Medicare and Medicaid Services (CMS) at the Federal level of about \$16.9 billion. As of April 1, they had drawn down \$7.96 billion of that or about 47 percent of the total amount of money that was available. They reported using the money to sustain eligibility requirements for the Medicaid population within the States and also to help them meet increased caseload demands. As we all know, during economic downturns, other people come on to the Medicaid rolls, and so they were able to do that.

Now, the Federal share increased quite a bit. In the States that we looked at, it went from a 7.9 percent increase in Iowa to an 11.5 or almost 11.6 percent increase in California. So the Federal shares increased significantly as a result of this legislation. That also may mean in some States they are able to reduce their share, thereby making funds available for other purposes. And some States have reported being able to do that and using that to avoid layoffs in other areas or to offset general fund deficits. And this helps to prevent other actions that might be detrimental to economic recovery.

Now, in the transportation area, money was made available to the 17 jurisdictions that we looked at, about \$15.5 billion. As of the middle of this month, about \$3.3 billion had been obligated. Now, obligated in this sense means that the Federal Government and the States have agreed on the projects to be funded. Many of these are still out for bid during the April and May time frame, while a few States, Mississippi and Iowa, among our sample, had actually let contracts to begin work. Most of the other States are in the process of completing the competitive bidding process and will then be awarding the money.

So far, there have not been a significant amount of Recovery Act funds spent yet for the highway programs, but as you mentioned, Mr. Chairman, the pipeline is there. The projects that have been agreed to by the Federal, State, and local governments for the jurisdictions we are looking at—there were over 950 projects that had already been approved. So this is moving through the system, and I think it will have the desired effect.

Now, in the State Fiscal Stabilization Fund, this is a new program, about 81.8 percent of the money in the State Fiscal Stabilization Fund is to be used for education purposes; 18.2 percent can be used for basic government services, including education. Now, about a little over \$20 billion had been allocated to the 17 jurisdictions that we looked at, but in order to be able to use this money, States have to submit an application to the Education Department. The Education Department reviews it, and then once the Education Department determine it is complete, the States can move forward.

Among the jurisdictions that we looked at, two have submitted their applications and have the review completed by the Education Department. Last Friday, the Education Department gave the OK to California, and this past Monday to Illinois. Other States are in

various processes of preparing their applications and submitting them to the Education Department for review.

Now, in addition to looking at the uses of the funds, we also looked at the efforts being made by the States to ensure that there are proper safeguards and proper accountability mechanisms put in place. Here, we were pleased to see the States paying very close attention to their new responsibilities. They were appointing people to focus on this program full time, either as a Recovery Act czar or special person associated with it. They were trying to assess what some of the internal control risks were up front, as you mentioned, Senator Collins. And there are some risks; some of the prior audit work and other things done note some areas where sub-recipients have not been monitored in the past as they need to be, but people were trying to put in place proper improvements to ensure that those risks were mitigated.

Now, here we found exactly what was mentioned by both of you, Senator Lieberman and Senator Collins, in your opening statements. Most of the States have been under fiscal stress and they have cut back, some significantly, in the amount of oversight activities that they are funding at their level, both in the management side as well as on the auditing side. So that is a concern that they had, and we recommended to OMB that it clarify where administrative funds can be funded through the Recovery Act. There are a number of possibilities. There are also indirect cost rates in some of the existing Federal programs. So we were pleased that OMB and the Vice President adopted our recommendation, and they are going to clarify that.

The other recommendation we made to OMB was to modify the Single Audit process. This is the State audit of the departments by the State auditors. It is a very important tool, but unless it is changed, as Senator McCaskill mentioned in our last hearing, and modified to allow for earlier testing of the program and to give some relief to the State auditors, it will not be a timely, effective tool, as much as it could be, to help with Recovery Act funding.

Now, our recommendations would mean the auditors would do some testing of internal controls in 2009, before a lot of the money is spent in 2010 and 2011. So it is very important. OMB has acted positively. We were hoping that they implement those changes.

We also made recommendations that OMB provide better clarity on the methodologies used to estimate the number of jobs created and preserved, which is a very important aspect of evaluating the impact of this program. And we also made recommendations that OMB move to improve the communications with the States, to give them more timely notice of the availability of the money, the application process. And importantly, a lot of States were concerned that they were not getting information about the amount of Federal money that would flow directly to localities within their State that would not come through the State agencies. So they would not have a total picture. That would impede their ability to assess the overall impact. So we made the recommendation to OMB that they provide that information to the States, and they have agreed to do that.

So, in closing, I just would say we have made a series of recommendations to OMB. They are acting on those recommendations.



We are very pleased with their response and also would want to publicly thank all the State and local officials, including the associations that are here today. But we have received very good cooperation in every State and locality that we have been in, as well as with our Federal officials. So we look forward to continuing our responsibilities under the Recovery Act, and we will produce regular reports as required. And I will be happy to take questions at the appropriate time, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much. You got us off to a good beginning. And I appreciate what you did, because I am sure there is a connection between the work that you have done and your communication with the Vice President's office and his announcement today about the guidelines that will make it easier for the State and local government.

Also, during the question and answer session, I want to come back to this because this is really quite interesting, and probably surprising to most people. One, much more of the money will be spent in Fiscal Year 2010 than this year. And then, two, a lot will be spent from 2011 right out to 2016.

Mr. DODARO. And, actually, some of it may even go further.

Chairman LIEBERMAN. I want to get into that a little bit—

Mr. DODARO. Sure.

Chairman LIEBERMAN [continuing]. During the questions and answers session.

Next is Ray Scheppach, who is with the National Governors Association. He has been here before, although not recently, and always welcomed. Thank you for your testimony this morning.

**STATEMENT OF RAYMOND C. SCHEPPACH, PH.D.,<sup>1</sup> EXECUTIVE DIRECTOR, NATIONAL GOVERNORS ASSOCIATION**

Mr. SCHEPPACH. Thank you, Mr. Chairman. Good morning, Senator Collins, Senator McCain, and Senator Bennet. I am pleased to be here on behalf of the National Governors Association (NGA) to talk about implementation of the Recovery Act.

My best estimate right now of the fiscal shortfalls in States is somewhere between \$200 and \$250 billion over the next 3 fiscal years, and that is the States fiscal years of 2009, 2010, and 2011. Because 49 out of the 50 States have a balanced budget requirement, they can only take two actions. One, they can cut budgets or raise taxes, both of which will have a negative impact on the economy. Because of that, it actually has a multiplier effect on the economy, making it longer and deeper. This is why many economists argue that one of the most productive strategies is to provide flexible money to State and local government to offset that negative action.

In terms of how much is coming to States, we estimate it is probably around \$246 billion that comes to States or through States to individuals out of the total \$87 billion. I tend to think of this money in four broad categories, or buckets, depending upon the intent and the timing of it.

The first category I would argue is the counter-cyclical funds, or the funds that are relatively flexible. I put the \$87 billion of Med-

<sup>1</sup> The prepared statement of Mr. Scheppach appears in the Appendix on page 328.

icaid money in there not because you can utilize the Federal money, but, again, because you can withdraw the State money that you had planned to put in there and move it to, in fact, plug holes other places.

The second component would be the State Stabilization Fund, that \$39.5 billion, really, plus the \$8.8 billion flexible money. And the reason that is relatively flexible is that education represents about 32 percent of State budgets, if you add higher with elementary and secondary. So because of that, you have a fair amount of flexibility to move that around across those various categories.

If you add those two categories together, you get about \$135 billion in relatively flexible money. And that is going to go a long way, and you are already seeing a number of States, basically, not go forward with planned cuts because they know that the money is, in fact, coming. And so I would argue, some of that is already having a positive impact by offsetting negative cuts.

The problem is, in all honesty, that even after that money, States are going to continue to have a shortfall in the neighborhood of \$200 billion over the next 3 years, which means most States are going to have to continue to downsize, consolidate, and/or raise taxes.

The second category I would like to talk about would be the straight appropriations, which is mostly the formula grants. This is the highway money and the sewer money. This is the energy grants, the weatherization, and so on, which is a little short of about \$100 billion in those funds. Most of it is in existing programs, so it can be at least obligated relatively quickly because the rules of the game are generally known. With the exception of those new programs or some programs where you have had dramatically increased budgets, I think those will go along fairly smoothly, and you will begin to see, shortly, outlays in a number of those programs.

The third category is what I call the safety net. That is essentially the food stamps, unemployment, and so on. That is about \$40 billion. And there is a fourth category, which I will argue is a longer term investment, trying to develop the foundations for economic growth in the longer run. I put the money in terms of alternative energy and smart grid, health information technology (IT), broadband build out, high speed rail, and research and development money into that category, where I think you actually have to spend somewhat more time in planning to ensure that money is actually spent efficiently.

In terms of the good news, I think there is a lot of good news so far. I would argue that the Vice President's office actually has provided a lot of leadership on this issue, and has been in touch with governors. And I think I would give the Administration, OMB, and agencies, pretty high marks in terms of getting out guidance as fast as they can, trying to get out the allocations so States know what they are going to get. So a lot of information has flowed already.

Second, I think governors have all designated their leads, and many of them have, in fact, appointed task forces or working groups. A lot of those have included private sector, local govern-

ment, and other organizations, so trying to get at some of that outreach that you were talking about.

Third, I think OMB and GAO have been very accessible. We actually have calls every Friday morning to talk about emerging problems and try to feed those back into OMB. And they have been very responsive about trying to deal with those issues as we find that they come forward.

Finally, I would say that most times, I would probably argue as an economist, that attempts to stimulate the economy through fiscal policies have generally failed. They have been too late. Generally, the money starts being spent after the economy is already recovering.

I suspect this time, you are probably going to be much closer to the mark. Again, I would say that already I see a number of States postponing cuts because they know the money is coming. That is having a positive effect on the economy. And I think over the next 2 to 3 months, we will begin to see some additional outlays from this package. And I can tell you that, as far as the revenues in States is concerned, it is still coming in month after month, the worst estimates. So we see no recovery yet or even leveling off in State revenues.

There are a number of challenges, I think, however, that governors have. The biggest one is that we do believe that this budget hole will be for 3 years. Two years because we probably will not get GDP back to the 2008 level for 2 years, and we know from the last three downturns, the biggest impact is on States in the year after the recession is declared over. And that is primarily because the Medicaid spending is very late. It takes time for people to lose their jobs and then apply for Medicaid, and so that spending is very late. And, of course, similarly, income tax revenues continue to fall very late in the cycle.

So governors are going to have this tension between spending the money now quickly to gain the job creations on one hand, and on the other hand, trying to maintain program stability and fill the budget hole that is going to last for 3 years.

The second one is there is a lot of accountability here, much more than is normal. Not only are governors going to be accountable to OMB and the agencies, but also now the Recovery Act Transparency Board, the inspectors general (IGs), and, of course, GAO, is out in the field. So there is a phenomenal amount of accountability.

The only issue there, I think, is that we hope that the data requests can be streamlined and that congressional committees also do not ask for separate information, which is happening in some instances, because it is not the oversight as much as it is the data collection that I think is potentially burdensome to the States.

You have already mentioned this issue of funding for this. I would argue that this has been one of the biggest issues, that there is no place to charge the additional work that is necessary. And so, to the extent that OMB and the Vice President's office is dealing with that issue, I think that is going to be very valuable.

I do think that this whole issue of collecting the number of jobs is going to continue to be difficult. I am not sure at the end of the day, even when we get more guidance, that the data is going to be

particularly usable to look across States or across programs just because of the difficulties in collecting accurate information.

The only areas that I think that there are going to be problems are when you are establishing a new program, that is something like in weatherization, where you may have gone from an appropriation level previously of \$200 million to \$6 billion. That is a phenomenal ramp-up, and I think it is going to be difficult to maintain program stability and efficiently at the same time as ramping up that program.

You have already mentioned the capacity problem. It is true, as Mr. Dodaro has indicated, States have cut back over the last couple of years, and, therefore, have less capacity in the accountability area, and, therefore, are going to have to build that up over time. It is also true that the existing information systems may not be the ones that can handle the new data requests, and, therefore, it may be that those are going to have to be reprogrammed, which will take time.

The only final comment I will make is that there is a lot of funding going to local government and to port authorities and other places, where governors do not have control over. They are concerned about making sure that they are at least informed when that money goes directly to other entities so that it is coordinated.

With that, Mr. Chairman, I would be happy to answer questions.

Chairman LIEBERMAN. Thanks very much. A very good and helpful report from the State level.

Next, we have Carolyn Coleman, who is here to represent and speak on behalf of the National League of Cities.

Good morning, and thanks for being here.

#### **STATEMENT OF CAROLYN M. COLEMAN,<sup>1</sup> DIRECTOR, FEDERAL RELATIONS, NATIONAL LEAGUE OF CITIES**

Ms. COLEMAN. Good morning, Chairman Lieberman. It is good to be here.

Also, good morning, Senator Collins. Good to see you again. I know the local leaders who were here in Washington a few months ago really appreciated your remarks at our conference.

Senator McCain, Senator Burris, and Senator Bennet, it is good to be here with you as well.

I welcome the opportunity to discuss this important issue with you. Local governments across the country are working very hard to plan and to be ready for the funds as they begin to flow a little bit later this year into our communities. Different from the remarks you just heard from Mr. Scheppach and the National Governors Association, we are estimating about \$40 to \$60 billion of funds will come to local governments. And it is not just cities and towns, but other local government entities in our States across the country. So we do not have quite the firm handle on exactly which funds, but we believe that is a good estimate.

It has also been clear to us, and becoming clearer everyday, that while these funds are welcomed and cities and towns will be able to put them to good use, that they will not begin to fill the budget holes and the stresses that are happening at the local level, given

<sup>1</sup> The prepared statement of Ms. Coleman appears in the Appendix on page 337.

what we have seen with sales taxes, property taxes, and income taxes. So while these funds will be helpful, much more will be needed to meet the budget gaps that are on the horizon for cities and towns.

We do believe that the transparency and accountability provisions in the Act will help ensure that we can get the maximum possible benefit out of these funds. And also, and I think importantly, that we will be able to best engender the American taxpayer's confidence in the ability of all levels of government to actually get things done in our communities. I want to assure you that in conversations that we have been having with local leaders everyday over the last several months, that they are truly embracing the accountability provisions and ramping up to move forward.

I want to talk just a little bit about what the National League of Cities (NLC) and other organizations have been doing to help local leaders get ready.

Senator Collins, you made the comment about it is not just local governments, but it is also nonprofits, the fire stations and others that are striving to understand, still, what is in the bill, what can be accomplished, and how do we access those resources.

We have been working very hard here in Washington to help them understand exactly how to do that. For example, NLC has hosted three recovery-focused Webcasts. Each Webcast is reaching 4,000 to 5,000 listeners. The demand is high and they are hungry for this information, and we will continue to do this. We do appreciate the ability that we have had to invite our partners here in Washington, the Federal agencies, and we look forward to OMB and GAO and others on those calls, so, again, that we can help get the information out to them quickly.

I mentioned that we had a conference here in Washington recently. We, at sometime in February, decided to really customize the programming for that conference so it was focused around the Recovery Act. So it gave us another opportunity. And I know that the other associations here in Washington did something very similar to make sure to get the information into the hands of the people who had to make this work.

I think probably the most important discovery that we have embarked on lately, another initiative, is the recovery coordinators network. We have invited about 50 to 60 local government czars to convene in a forum where they can exchange ideas, find out what is working, what is not working, where they are having obstacles, where can they, perhaps, implement some self-help and get some solutions to some of the challenges in terms of moving forward with the Recovery Act. And I could tell, based on just an hour phone call with them yesterday, that while they are moving forward, they do share some of the same concerns we have heard this morning from you, as Senators, as well as from Mr. Scheppach, and from GAO, that the capacity issues and the stress on the current infrastructure and local governments is going to be tough. And what we certainly do not want to see is governments making decisions not to pursue recovery funds because they are afraid that there will not be the administrative dollars to help manage those grants effectively. I think that is just the course of actions that we do not

want, to leave these dollars on the table when they are so needed in our communities.

We are convinced at this point that OMB, the Federal agencies, and the Vice President's office—and you have heard this before—are doing a great job in terms of the spirit of cooperation. We know that this is an emerging process, but I think it has been working very effectively in terms of not only our ability to reach out to them with questions and to consult with them as they develop new guidance, but also for them to reach out to us and to the local governments and try to give information that will be helpful.

I am going to talk just a little bit about some of the mechanisms that cities and towns are putting into place in order to comply with accountability and transparency provisions of the Act.

Many of them, just like the Federal Government, have been launching their own recovery Web sites on their own home pages. And, for example, I am going to give you just a few of the jurisdictions that have been doing this, but I can assure you that many of them have launched their own Recovery.gov Web sites. But Hartford, Connecticut, has launched one; Lewiston, Maine; Reno, Nevada; Kansas City, Missouri; Detroit, Michigan; Denver, Colorado; as well as Chicago, Illinois, have launched Web sites that are making it a little easier and a little more transparent for not only citizens but also vendors in their communities to understand how to access these resources and to understand the process that the city will use to allocate those dollars. And I think we will begin to see more of those as we go forward.

In terms of how cities are organizing themselves to oversee the implementation of the Recovery Act, as you might suspect, it has not been a one size fits all. We are basically seeing a couple of different models, with some cities establishing the recovery czars and the mayors appointing a recovery working group. That could be just city staff. It might also involve members of the private sector. That is one model.

Then the other model we are seeing is a little less centralized approach, where the mayor's office might be overseeing the recovery implementation, but the individual city agencies are making the decisions about which funds they will apply for. I think it is important, then, we just have to recognize, with the many different types of governments and sizes of local governments that are involved and pursuing funds to the Recovery Act, that they will have to customize their internal bureaucracy to best fit the needs of the Act as well as their city.

I do want to echo—and this has been mentioned before—that there are lots of questions, and there continue to be questions, in terms of what is a job created, what is a job retained, and how do we track those. So like the other comments you have heard on the panel this morning, cities and towns, too, would welcome additional guidance that we believe will be forthcoming from OMB on that important topic.

I just want to briefly echo—and I have mentioned this already, and I share this with the others who have talked before—we would welcome and look forward to the additional guidance from OMB in terms of the administrative costs and getting some additional funds to do that good work.

I believe that covers many of the areas that I wanted to mention this morning, and I look forward to the questions from the panel. And I just want to say that we look forward to continuing to work with the Federal agencies, with OMB, the Vice President, as well as with the States and the other organizations here in Washington to make this a success. Thank you.

Chairman LIEBERMAN. Thanks very much, Ms. Coleman, for that testimony.

We will do 7-minute rounds of questioning. And there are two elements of our interest. First, is the money being spent rapidly enough? And then, second, are we setting up mechanisms to monitor how it is being spent to avoid waste and fraud?

Let me begin on the second question with the Vice President's letter this morning, and just try to develop that a little bit, Mr. Dodaro.

In the letter itself, it says that the OMB guidance will provide for "new flexibilities for States for cost of administrative activities associated with the Recovery Act."

So help us understand, because your work, I think, has been a big part of generating this letter, as well as concerns and realities expressed from the State level.

Is it the flexibility for overall Administration funding for the State and local governments or is it primarily money to audit or oversee this funding?

Mr. DODARO. It is basically, from a management perspective, to oversee the programs. It is not on the audit side. Now, the audit side is a concern.

Chairman LIEBERMAN. Right.

Mr. DODARO. And our recommendation, though, basically, on the audit side, Mr. Chairman, would be to give the auditors flexibility to reallocate their resources from low-risk areas to the Recovery Act areas and focus more on high-risk areas.

Chairman LIEBERMAN. Federal auditors or State—

Mr. DODARO. State and local auditors.

In 1984, there was a mechanism put in place called the Single Audit Act for State and local auditors to audit their entire entities, including Federal funds, and there is certain testing. And that is a foundation accountability tool that has been put in place. And it is a very effective tool, but it could be modified. But if it is not modified, it is going to be too late, because they will not look at a lot of this until 2010 is over. This gives flexibility up front and reduces the amount of money that would need to be spent.

Now, if they do not want to give the State and local auditors flexibility, then they should give them additional money to cover this earlier. But most of what the Vice President is talking about deals with giving States the management capacity, people administering the program—

Chairman LIEBERMAN. So, for instance, the people administering the Medicaid program or State transportation programs.

Mr. DODARO. Yes. Or in the administrative areas, the procurement people, the people to monitor sub-recipients in the program areas. It is those type of people that have been cut back as well.

Chairman LIEBERMAN. Incidentally, I noticed that Congressman Ed Towns, who chairs our partner committee in the House, the

Committee on Oversight and Government Reform, is proposing legislation to separately fund State and local auditors to oversee stimulus spending.

What do you think about that?

Mr. DODARO. Well, that is an important proposal that I think could work. Our proposal is intended to minimize the amount of additional funding, but the additional funding is very appropriate, commensurate with the amount of additional Federal resources that are going to go there. So I would be supportive of that. I think that is very important.

Chairman LIEBERMAN. Do you have any idea about the amount of money it would require?

Mr. DODARO. Not offhand, but I could provide an estimate.<sup>1</sup>

Chairman LIEBERMAN. Please do that, and we will be in touch with Congressman Towns. I have no idea whether it is even plausible to think about that, but I am interested in the idea.

Let me go to the spending side now, because I think one reaction to that chart would be—well, let me define the chart first.<sup>2</sup> This is under the Stimulus Act. This is just the money going to States and localities, right?

Mr. DODARO. Yes, that is correct.

Chairman LIEBERMAN. What does not it include?

Mr. DODARO. It does not include the \$280 billion in estimated tax relief provisions, and it does not include direct—

Chairman LIEBERMAN. And payroll taxes are not included.

Mr. DODARO. Right. It includes about \$280 billion of the \$787 billion estimated amount for the Recovery Act.

Chairman LIEBERMAN. So on that chart, what jumps out at me, certainly, and I presume would at others, is that a relatively small proportion of that money is going to be spent in this fiscal year.

Mr. DODARO. Well, I think, Senator, if you reflect on the fact that the Act was passed in February, we were almost halfway through Fiscal Year 2009 before the Act was passed. So there is only about 7 months of spending in Fiscal Year 2009. So if that was extrapolated, you would have a greater figure, but I think that is part of the reason for that.

Chairman LIEBERMAN. So you are not critical, at this point, that the Federal Government is putting this money out too slowly. In other words, your attitude—I do not want to put words in your mouth.

Mr. DODARO. Right.

Chairman LIEBERMAN. One would look at that and say, how come so little is going out this year and so much more in the next 2 years, when we need it now, people would say.

Mr. DODARO. Well, I would say two things. One, I agree with Mr. Scheppach's comment, that because the States know the money is coming, they are able to take action to avoid making some cuts right now.

Chairman LIEBERMAN. Right.

<sup>1</sup> The response from Mr. Dodaro appears in the Appendix on page 652.

<sup>2</sup> The chart referenced by Senator Lieberman appears in the Appendix on page 326.



Mr. DODARO. They know they will have a steady stream of payments, for example, in the Medicaid area, which is a large portion of this funding, so they can plan accordingly going forward.

I think particularly for areas that are new areas, like the State Fiscal Stabilization Fund, the balance between spending the money wisely with the proper amount of controls in place is being balanced appropriately with due speed to get things out. In the transportation area, there was a lot of planning in advance of passage of the Act by the State departments. They are focused on construction and maintenance before they can get the contracts out right away.

So I think it is proceeding in a balanced fashion, where we will both get the money out as quickly as possible, but wisely and with the proper degree of accountability, so we will get the right result at the end.

Chairman LIEBERMAN. Obviously, you will keep monitoring and let us know if you think that it is moving more slowly to State and local governments than it should or could.

Am I correct that if you did a chart—and I would not ask you to do that today—of all money being spent under the Stimulus Act, including tax relief, unemployment checks, and reduced COBRA premiums, that a greater percentage would be spent this year, or am I wrong?

Mr. DODARO. My staff tells me, yes. CBO has already produced that in scoring the bill, so we can provide that.

Chairman LIEBERMAN. Yes. I would appreciate that. I did note, in the hearing we held in Connecticut a couple of weeks ago, that the State budget director seemed very pleased with the Federal Government's interaction with the State, but ultimately said that money had been obligated, but they actually had not seen any money yet. But they were reassured that it was coming, and as a result, they were not laying some people off that they thought they would have to.

Mr. DODARO. That is exactly right, Senator. And that is what we have seen across the States that we visited.

Chairman LIEBERMAN. Right. I am over my time. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Dodaro, in the last hearing, we talked about the importance of the accurate and agreed upon measures on the number of jobs either created or retained. The Administration has estimated that more than 3 million jobs will either be saved or created by this Act. That, arguably, is the most important measure of the effectiveness.

Two other witnesses today have commented on how difficult that measurement is. I brought up in the last hearing the concerns of my State officials about whether, if you are creating a construction job for 3 months, and then that person goes on to another construction job that is funded by this Act, is that two jobs? Is it one job? Is it a job created in the first place and then preserved?

I know in response to the concerns that we raised at the last hearing, that OMB has put out additional guidance. Do you think that guidance is accurate as far as allowing us to assess how many jobs really were created or saved by this important bill?

Mr. DODARO. I think the guidance was a good first step, but it does not go far enough. And that is what we heard from the States and localities that we visited.

To deal with the question that you mentioned, they try to deal with it in a full-time, equivalent type discussion, so you do not do double counting. But you also need to have a way to measure the indirect effect on employment or the multiplier effect, as Mr. Scheppach, and other economists would say. So we recommend in this report that they develop additional methodologies to try to get a consistent reporting approach so that the proper amount of information can be gathered to draw the conclusions that you and others seek to find.

So we think additional guidance is necessary. We think a cooperative effort at the Federal, State, and local level is warranted. And I believe OMB agrees, and we will be trying to move to develop additional guidance.

Senator COLLINS. I think that is so important in terms of credibility and also uniformity, because it cannot have one State doing it one way and another doing it a completely different way.

Mr. Scheppach, I want to follow up on a comment that is in your March 10 report on State implementation of the Recovery Act. You made a very interesting point in that report about the new law having several "use it or lose it" provisions, which require State funding to be allocated to other States if they are not obligated by a certain deadline.

Now, I am not talking about those few States that have decided to refuse recovery funds altogether. I am talking about States that have accepted the funds but now face deadlines to expend the money.

Several years ago, I headed an investigation into fourth-quarter spending in the Federal Government, and we found that the "use it or lose" mentality causes money literally to be shoveled out in wheelbarrows because of the fear that it would not be available. It led to a lot of wasteful spending.

There is a balance here, a tension between our desire to make sure that the money is being spent quickly so it stimulates the economy in a timely fashion, a point you made in your opening remarks. But there is also the concern that if there are deadlines for spending it, that the money may be just put in that wheelbarrow and shoveled out, and not spent wisely.

Could you comment on what you think we could do to ensure that the use it or lose it requirements do not lead to wasteful spending?

Mr. SCHEPPACH. I would say right now, when you talk with the leads who are basically administering this money, they are very scared because of all the oversight; that I am not sure you are going to see that this time at the end of the queue because nobody wants a story in the local newspaper, or down here, that money went out inappropriately.

So my own view is that until we get to that point, that money is probably going to come back to Washington, and it is going to be redistributed. I do not think anybody out there in States right now is going to take any risks with accelerating that money.

Senator COLLINS. Thank you.

Ms. Coleman, you mentioned that your organization is doing Webcasts to help educate local officials, and I really commend you for that because this is in some ways a bewildering maze for smaller communities to try to follow. I want to give you a specific example and see if you have some suggestions.

There is a small fire department in Maine, the Readfield Maine Fire Department, that was looking for a potential source of funding under the Recovery Act and could not determine a source, based on the information available. This fire department went to the State's Commissioner of the Department of Administrative and Financial Services, who found that there were 30 different Web sites that potential Recovery Act funding recipients would have to access to find funding that they might be eligible for.

Now, it turns out for this fire department, there is a pot of money in the Federal Emergency Management Agency (FEMA) that we increased by \$200 million that would meet its needs. But how is a small fire department going to figure that out if there are 30 separate Web sites that need to be accessed?

We focus so much on oversight and transparency, but do you think that more needs to be done to help the potential recipients of money determine how to apply and where the money is located?

Ms. COLEMAN. That situation or scenario you describe is happening across the country, and it is, in part, why the national local government associations and the State affiliates of those organizations, are working very hard to educate and make information available to local city leadership so that they know more quickly and do not miss deadlines, and do not leave money on the table, so they can find out what is it that we could use to fund this need in our community.

On top of that, there is no one place, yet, where you can find all of the funding opportunities for cities in the Recovery Act, so that is being cobbled together. But it is a particular challenge, and that is why we want to continue using the technology via Webcasts, conferences, meetings out in the various cities and towns.

I know some State associations have been hosting townhall meetings and inviting representatives from the different Federal agencies, using the regional offices of the Departments of Housing and Urban Development (HUD) and Homeland Security, and inviting those representatives into a townhall meeting in communities where the public and nonprofit groups can then be on site asking these questions.

But I think it will continue to be a challenge. And I go back to, if recovery is to be successful in cities and towns, the first most important thing we need to do is help educate our local leaders so that they know what is possible and how to get to those resources. But it is a challenge.

Senator COLLINS. Thank you.

Chairman LIEBERMAN. Thanks, Senator Collins.

I will call on Senators in order of arrival, which today is Senator McCain, Bennet, Burris, Carper, and McCaskill.

Senator McCain.

### OPENING STATEMENT OF SENATOR MCCAIN

Senator MCCAIN. Thank you, Mr. Chairman, and thank you for holding this hearing today. It is obviously very important that we do the best we can to monitor the expenditures of these large amounts of funds.

Mr. DODARO, much of this funding has been expended, and it is being expended, for State expenditures for Medicaid services.

Is that pretty much across the board to make up for deficits that the States are experiencing? Is that what you are finding out?

Mr. DODARO. Senator, the Medicaid money, the way that the Act worked is that it gave each State a 6.2 percent increase in the Federal matching rate, and then depending upon the unemployment rate in the State, there is an additional match, additional funding. The States that we visited, for example, Iowa received a 7.09 percentage point increase in the Federal match. California is 11.60 percent.

Now, the underlying theory here was to give fiscal relief to States, but also to help them meet increased caseloads and to maintain eligibility requirements. So the States have to use the Federal money for Medicaid services. They have to maintain eligibility requirements that were in place as of June 2008. So they cannot reduce the eligibility requirements. They have to continue to pay providers promptly in order to continue to receive the money, and they cannot use any of the money to put into a rainy day fund within the State.

Senator MCCAIN. Isn't it true that some States' eligibility rules on Medicaid has prevented them or hindered them from getting this money?

Mr. DODARO. I believe there is one that had to go back and restore some of the eligibility requirements to get the money, but they have to maintain the eligibility requirements that were in place in June 2008.

Almost all the States that we have looked at have drawn down the money, Senator, except for Colorado. Colorado had not, among the States, drawn that down. So that is one of the areas that we and the inspector general are going to continue to look at, is to make sure that the States meet the maintenance requirement and eligibility standards. I am not aware of any particular situation.

Senator MCCAIN. I see.

I was looking at your table number 4 here,<sup>1</sup> which shows the percentage of apportionment that has been obligated by the various States. It is a part of your report, I believe, on page 19.

Mr. DODARO. Yes.

Senator MCCAIN. The thing that kind of interested me here is that at least one State, Iowa, has obligated 62 percent, and yet there are several States that have obligated zero. What is the story here?

Mr. DODARO. Well, in some States, the legislatures have to approve the projects before moneys can be spent. And that is the case, for example, in Florida that you see here, that has—

Senator MCCAIN. Zero.

Mr. DODARO [continuing]. Zero. So every State is set up different.

<sup>1</sup>The table referenced by Senator McCain appears in the Appendix on page 307.

In some cases, the transportation department is not even under the governor's authority, like in Mississippi, for example. So depending upon the State's structure and what the rules are in terms of the legislatures having to approve the funds, that dictates in large part the pace that you see here and the differences among these States.

Senator MCCAIN. So it is really a matter of procedure rather than lack of action that has gone on here, in other words?

Mr. DODARO. That is correct. It is the process within the State to commit to be able to move that forward, and it varies. All the ones that we looked at were planning and are trying to move forward. It is just a matter of going through their proper, normal process.

Senator MCCAIN. And according to your chart there that we are looking at, we would anticipate by the end of 2010 to have dispensed roughly about 60 percent of the funds?

Mr. DODARO. Yes, to the State and localities. Right.

Senator MCCAIN. And what are the major problems that you have found the States are encountering?

Mr. DODARO. Major problems are, first, having clarity, guidelines, on whether they can use some of the moneys to increase their oversight and accountability mechanisms. And we make a recommendation to OMB that they clarify that so the States can deal with that issue.

Senator MCCAIN. Have you found that in some areas, that apparently there are insufficient mechanisms in place for oversight?

Mr. DODARO. Yes. We think that in some States, they have cut back considerably on their oversight. That heightens the risk. I mean, we have not seen actual problems yet because of the status of the money, but I am concerned, based upon their analysis of where some of the risks are. And unless they move to address those risks, we could have problems down the road.

Senator MCCAIN. I interrupted you, by the way. Do you want to complete your answers?

Mr. DODARO. Yes, right. On the second area, Senator, there is greater need for communication at the State level about what money is going directly to the local government, bypassing the States. So we have recommended to OMB they clarify that, and they have agreed to do that.

Third, States need some guidance on methodologies and definitions for the number of jobs preserved or created, and the total amount of data collection requirements that are being imposed on them. And we have made recommendations in both of those areas in our report today to address that. And OMB understands those issues and hopefully will move to clarify them.

Senator MCCAIN. Ms. Coleman or Mr. Scheppach, do you have any comment on those questions that I asked Mr. Dodaro?

Mr. SCHEPPACH. Well, the only thing I would say on the Medicaid issue is that the Medicaid was the one area where the payments are actually retroactive to October 1, 2008. So it seems to me that Congress intended by that to provide some money early to offset potential cuts that States were going to make. And I think that was very helpful. I mean, most of the money that is, in fact, going

to pay out in 2009 I am assuming is the Medicaid money. So it is the fastest money that will be going out.

Senator MCCAIN. Not exactly the largest job creator. Ms. Coleman.

Ms. COLEMAN. Senator McCain, I would just echo what GAO has said. We also look for additional guidance and clarity around the performance measures, the data management requirements, and greater communication about where dollars are going, not just States and locals, but just overall.

Senator MCCAIN. Thank you. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator McCain.

Next is Senator Burris. Senator Bennet has left.

#### OPENING STATEMENT OF SENATOR BURRIS

Senator BURRIS. Thank you, Mr. Chairman, Ranking Member Collins, and other colleagues on the Committee.

I would like to welcome our distinguished panelists and certainly have some major concerns. I just hope that my concerns can be addressed by this panel.

Having been home over the recess, and when I go home on Saturday, I am getting confronted with questions about where the stimulus money is going. Primarily in the minority communities, and specifically in the black community, I want to know whether or not any of the Federal guidelines, for example, on that transportation money, when it is going to the States, whether or not those States have to follow any type of guidelines with reference to those minority requirements, that those moneys be shared with minority companies and small businesses.

Any one of you want to respond to that? Mr. Dodaro, if you would like to, or the governors. I have some more questions down that line as well.

Mr. DODARO. Right. In the transportation area, they basically use the existing Federal highway program, but there are some new requirements. One is that the States have to maintain their level of spending and have to certify that they will do that in order to continue to receive funds, and that they give priority to economically distressed areas.

Now, those two areas we are going to look at more carefully in our subsequent reviews to make sure that they comply with those requirements because we want them to get through their process to designate the full range of projects that they are going to fund in those areas.

But as I mentioned, and we discuss in our report today, there has not been a significant amount of money allocated yet, or spent yet I should say, in the transportation area, with the exception of a couple of States, Mississippi and Iowa. Most of the projects now are out for competitive bid.

Senator BURRIS. I understand Illinois has been allocated \$187 million in transportation dollars. I do not know whether or not the dollars have come. And then they had all these 5-year projects, and that is where the dollars are going, to those projects. The reason why Illinois got the money so early—

Mr. DODARO. Right.

Senator BURRIS [continuing]. Is because we already had projects. And the question is whether there are any stipulations on those projects, because that is all I am hearing. The stimulus money is coming to Illinois, and the small businesses are saying where is it going, who is getting it. I know it has to go through the States, it has to go through the legislature to be appropriated.

But were there any other special guidelines that would deal with that for smaller, minority companies, other than those standards, which mean that it would be very little dollars getting into those companies that are going to need it.

Mr. SCHEPPACH. Yes. I would just echo. I think what the law requires is the normal standards that have been in place for all transportation spending and all spending. And then, second, in the transportation area, you are supposed to give preference to distressed areas. But it is true that there is very little money that has been obligated in States yet, so it is hard to say what is happening.

Senator BURRIS. So we will be able to track those and determine what is happening there?

Mr. DODARO. Yes.

Mr. SCHEPPACH. There are very detailed requirements in the Act for States to report on a quarterly basis of exactly where that money goes for every specific contract.

Senator BURRIS. Well, I was looking at a figure in Illinois, having received \$15 million for the Illinois Health Center funding. And there were 36 projects, and the data is there. And I am looking at some of these clinics and health centers that are on the money for allocation. And I am just wondering, is there oversight responsibility as to whether or not those clinics are in underserved communities? And if they are not, then what type of penalty or requirement would be faced on these States, or the local government, whoever is responsible for allocating those moneys to these health centers, if they are not giving money to health centers in underserved areas?

What is the punishment if they do not? The money will then be out and spent and will not be shared.

Mr. SCHEPPACH. Well, first off, I think that in most categories, you are required to come back to the Federal Government with specific projects that are going to be done, to be approved at that particular level. So there is some additional oversight there as well. I do not know of any penalties, but I can tell you, most people who are dealing with this money do not want to make errors because they know they are going to be called out publicly.

Senator BURRIS. Pardon me, Doctor. It is not a matter who is dealing with the money. What my constituents are going to—how this stimulus money is going to impact the black community, in Chicago, in Peoria, in Rockford, and what Federal authority would we have to make sure that there is sharing of these stimulus tax dollars that are supposed to be stimulating these underserved communities?

Yes, Mr. Dodaro?

Mr. DODARO. Yes. Senator Burris, in the transportation area—this is with projects—in Illinois, our work has shown that they were apportioned \$936 million, and that they have obligated, which is the Federal Government and the States have agreed on 214

projects—this is as of April—that account for about \$600 million of that amount of money.

Senator BURRIS. Those are the 5-year plans and 10-year plans that the Department of Transportation (DOT) has in place.

Mr. DODARO. Right. That is exactly right. So for those 214 projects, the States has to follow the normal rules to make sure that they give attention to contracts for disadvantaged areas, disadvantaged businesses, rather.

Senator BURRIS. Right.

Mr. DODARO. And then there is also the additional requirement for economically distressed areas.

So part of our job will be to follow up to see—once these projects are in place and once the other ones are there, there should be a proper reporting back by the States. And we will be able to look to see whether or not they have met those requirements.

Senator BURRIS. Yes, but there is nothing—if they do not do it, and there are no requirements, and the money has been spent and has gone to all these major construction companies, and they did not meet the guidelines, is there a penalty to be paid?

Mr. DODARO. Well, there are additional projects in the pipeline that the Federal Government would have the ability to not approve, and there may be some other issues. These are not all the projects. There have to be additional projects. So I think there is supposed to be oversight by the Department of Transportation.

Senator BURRIS. But wouldn't we do better if we could get some type of upfront requirement before that money—whether or not the Federal Government would have any authority to oversee prior to the signing to rebuild I-75.

Mr. DODARO. Well, in this case, Senator, the Federal Government has approved these projects reviewing exactly what they have looked at is something that we need to do. But there is a check in the normal process that the State cannot go forward with the bids until the Federal Government approves the project. So all the ones I mentioned here, DOT has signed off on.

Senator BURRIS. I see my time is up.

Mr. Chairman, I do not know whether or not there will be a second round, but I have a lot more questions in this regard.

Chairman LIEBERMAN. OK.

Senator BURRIS. So if there is a second round, I would like to stick around and raise these questions.

Chairman LIEBERMAN. Well, we will see how the clock goes.

Senator BURRIS. We have to vote today I understand, too, this morning.

Chairman LIEBERMAN. The rumors are mixed. I guess it has been vitiated. They originally thought we were going to have a vote, but I think it has been vitiated.

Senator BURRIS. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator Burriss.

For the sake of clarity, Mr. Dodaro—because I know some of us have been affected by that chart. But it is clearly labeled. This is the pace of spending for State and local funds. But just to clarify, that is basically what GAO is charged to do here in oversight of this stimulus bill. Am I right?



Mr. DODARO. That is one of our responsibilities. We have other responsibilities. For example, to review the recipient reports once they come in; special attention to jobs created and preserved.

Chairman LIEBERMAN. Right.

Mr. DODARO. We have been required to look at special education grants.

We issued a report last week on the Small Business Administration's efforts to increase liquidity in the secondary market for small business loans.

Chairman LIEBERMAN. I did not mean to interrupt you, because I do not want to take——

Mr. DODARO. But I have the numbers on the total amount of the Recovery Act.

Chairman LIEBERMAN. Oh, you do? That is great.

Mr. DODARO. Yes, I do.

Chairman LIEBERMAN. Because that is somewhat beyond what you are doing; am I right?

Mr. DODARO. Right, that is correct.

Chairman LIEBERMAN. It is probably better for us to ask OMB, but since you have them, let us hear from you.

Mr. DODARO. Right. For Fiscal Year 2009, it is \$185 billion; \$400 billion in Fiscal Year 2010; and \$134 billion in Fiscal Year 2011.

Chairman LIEBERMAN. That is the total spending.

Mr. DODARO. Right, estimated total Recovery Act impact outlays.

Chairman LIEBERMAN. And that includes, for instance, the payroll tax cuts.

Mr. DODARO. Yes.

Chairman LIEBERMAN. That is surprising that it is still——

Mr. DODARO. But I think you always have to keep in mind that Fiscal Year 2009 is only half of a year.

Chairman LIEBERMAN. Yes, exactly. On October 1, we are starting the new fiscal year.

Mr. DODARO. Right.

Chairman LIEBERMAN. OK.

Mr. DODARO. So you only really have, from February 17 to September 30 in the 2009 numbers.

Chairman LIEBERMAN. So I suppose in fairness, as we judge the impact—I am thinking of Mr. Scheppach's statement that the history of fiscal stimulus is not always a happy one because a lot of times the moneys arrived after the economy has begun to recover. So \$185 billion is not small change, but the real impact is going to come after October 1 of this year. And I suppose, in that sense, in fairness, we are not going to be able to judge the impact of the stimulus until then.

I guess from our point of view—and I am going to stop here because I want to yield to Senator Carper—the question that we will always ask is if we are getting this money out as quickly as we can. Because, clearly, there is a desperate personal need for it around the country to get the economy going.

Yes, go ahead, Mr. Scheppach.

Mr. SCHEPPACH. Just to make a comment, you have to remember, though, that unemployment peaks very late in this cycle.

Chairman LIEBERMAN. Right.

Mr. SCHEPPACH. So we are probably not going to get to the 10 percent unemployment for another 12 months to 15 months. So I think that the amount of money that you have going out in 2009 and 2010, I can assure you, history is going to write you well, Senator.

Chairman LIEBERMAN. Well, that is very kind of you. [Laughter.]

Senator COLLINS. I wish Senator McCain had been here to hear that. [Laughter.]

Chairman LIEBERMAN. This reminds me of a great Churchill quote—which I am paraphrasing. But somebody asked him, after the end of World War II, how he thought history would treat him. And he said he thought history would treat him well because he intended to write it. [Laughter.]

So I thank you for writing it here this morning.

Senator Carper.

#### OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. Speaking of Churchill, Dr. Scheppach, were you the head of the National Governors Association when——

Mr. SCHEPPACH. When it began.

Senator CARPER. I was going to go back in time when George Voinovich was the chairman.

You were, were not you?

Mr. SCHEPPACH. Yes.

Senator CARPER. How about when Bill Clinton was chairman?

Mr. SCHEPPACH. Yes.

Senator CARPER. How long have you been there now?

Mr. SCHEPPACH. About 25 years.

Senator CARPER. That is terrific. You have done a great job. We are grateful to you. All of us are grateful to you.

Mr. SCHEPPACH. I have trained a lot of senators.

Senator CARPER. And one or two governors. And at least one president——

Mr. SCHEPPACH. Yes.

Senator CARPER [continuing]. When you think about it.

I got here too late to hear Mr. Dodaro give his testimony, but I am curious. I would just ask you and Ms. Coleman, did he use notes today?

Mr. SCHEPPACH. Did he?

Senator CARPER. Yes.

Mr. SCHEPPACH. No. He memorized it all.

Senator CARPER. He never uses notes. And I am told Churchill used to memorize his speeches. And once, I think, in an address he was giving before Parliament, he lost his train of thought in the middle of a speech, and he never memorized his speech again after that.

So I just want to be on hand when Mr. Dodaro is right in the middle of one of his testimonies and just loses it, entirely.

Mr. DODARO. Not yet. [Laughter.]

Senator CARPER. Well, you keep coming back and we will keep coming back. It is always a pleasure to hear your testimony.

I have three hearings going on at the same time, so I am going to slip out here in a minute.

Will you just give me the most important take-aways from your testimony, please, for our purposes today, each of you.

Mr. DODARO. Basically, the States are taking their responsibility seriously. They are trying to move through their processes as quickly as they can. They are concerned about their ability to provide proper accountability and oversight over the areas.

We made a series of recommendations to OMB to make the Single Audit process more effective, and we think that will help with accountability; to clarify how much Recovery Act money or what Recovery Act money can be used to strengthen the States' oversight and accountability mechanism is very important. The OMB needs to provide additional guidance to help people determine the amount of jobs created and preserved so we have credible estimates down the road. And they need to improve their communication with the States and localities to help them plan better. They are doing a good job. They are off to a good start, but they can build on that and do better.

Senator CARPER. Good. Thank you. Dr. Scheppach.

Mr. SCHEPPACH. It is very early now, so it is hard to say. The reports by States are not even due until October for the first one. But I think there is a lot of good cooperation. We are getting the guidance that governors need and moving forward.

You have to understand, though, that as much help as there is for States to offset the draconian cuts, that States are still going to be in a big hole for the next 3 years. And they are going to have to continue to cut and/or raise taxes in the order of magnitude of \$200 billion over the next 3 years.

Senator CARPER. Yes. Ms. Coleman.

Ms. COLEMAN. Senator, I would echo that we are off to a good start. The spirit of cooperation between the States, the Federal Government, the local governments, OMB, the Vice President's office, and others, I think, is going well. The local governments continue to get ready and are internally organizing their systems to be prepared to handle these resources. But we do share the concern about the resources to oversee these programs and to manage the grants effectively and in the manner that was intended.

I would also share what the governors have mentioned, that while these resources will be helpful, that the gaps will continue to be big at the local level in terms of our budget.

Senator CARPER. Well, they certainly are in Delaware, I can assure you.

I realize that the legislation is fresh, the money's just beginning to be dispersed, and the systems are set up to make sure States go out and get as much as they are eligible for and put the money to good use.

What do we need to be doing here in the legislative side, in this hearing? We are actually doing a series of oversight hearings, which would seem to certainly be appropriate given how much money is involved.

What should we be doing to exercise our appropriate roles?

Yes, Mr. Dodaro?

Mr. DODARO. Senator Carper, we made these recommendations to OMB about modifying the Single Audit legislation and also Senator McCaskill had mentioned this issue before. We followed up, as

she requested, and made these changes. And also clarifications on the administrative expenses.

There has been a bill introduced on the House side to give funding to the State auditors to carry out responsibilities. I would say, if OMB has not made the proper clarifications soon, that Congress may want to consider legislation to strengthen the ability of State oversight mechanisms, both to manage it, provide proper controls, and also audit it at that level, and, also, on the creation of a different approach or a uniform approach for job measurement on jobs created and preserved.

So I would wait to see what OMB does, if they take the proper action. I do not have any suggestions additionally for Congress at this time.

Senator CARPER. Do you recall who is the author in the House of Representatives of the Single Audit Act?

Mr. DODARO. It was 1984 when the Act was originally passed, and we made the last set of amendments in 1996.

Senator CARPER. An at-large congressman from a small State on the East Coast.

Mr. DODARO. Great foresight. [Laughter.]

Senator CARPER. I do not know. Let me follow up on that. State auditors already bear a significant responsibility for oversight of Federal spending by State agencies, pursuant to the Act and to the amendments that have been made to it. Those audits are generally conducted annually. They provide some assurance to the Federal Government as to the management and the use of funds that the States receive, as well as their subdivisions.

The importance of the Single Audit process is, I think, magnified, rather than minimized, by the Recovery Act's emphasis on accountability. And given the additional responsibilities now given to State auditing agencies, what plans are in place—and you spoke of this, but what plans are actually in place to ensure that these efforts are coordinated with Federal agencies?

Finally, what is being done by the Federal Government to increase outreach and coordination and communication with the State and local audit community, and to determine ways of improving data sharing?

If you would just comment further on that, I would appreciate it.

Mr. DODARO. States are in the process now of going through their planning activities for the Single Audit program. And the concerns that we have raised and, as I mentioned, Senator McCaskill had, and others before, was that the States right now, unless they adjust the process and it follows this amount of money—we think the Single Audit Act can be used more effectively to test controls before these expenditures are made in 2010. That will not happen unless OMB modifies the guidance. We will get the reports after all the money has been spent in 2010. And they could give them more flexibility to focus on the Recovery Act and less on low-risk programs as they know. So that is what we would suggest in that particular area.

Now, in terms of sharing responsibilities, soon after the Act was passed, sharing information, I had a conference call with 40 some State auditors. I followed that up at Senator McCaskill's request.

Senator CARPER. Was she a former State auditor?

Mr. DODARO. Yes, we have regular contact with the State auditors. They were one of the first places we stopped in the 16 States and localities that we visited. We are also working with the IGs and the Recovery Accountability and Transparency Board to coordinate all the audit activities.

We are also working with the National Association of State Auditors, Comptrollers, and Treasurers, and other groups, on the reporting requirements with OMB. And as Dr. Scheppach had mentioned previously, we have regular meetings every Friday to coordinate. So there is a lot of coordination going on. I am a big believer in that. I think it is very important early on this process.

Senator CARPER. Well, I applaud those efforts and urge you to continue them.

Let me just say to each of you, thank you for being here. It is a special privilege to see Dr. Scheppach.

Chairman LIEBERMAN. Thanks, Senator Carper. Senator McCaskill.

#### OPENING STATEMENT OF SENATOR MCCASKILL

Senator MCCASKILL. Thank you. This will segue nicely into what you were just talking about, Mr. Dodaro.

As a former auditor, I have looked at three programs in Missouri, and I know that the State auditor's office in Missouri is aware of this. But I will tell you where I think we are going to have a big, huge problem.

We have a weatherization program that in fiscal year 2008 received \$6.1 million. It is going to get \$125 million. We have a Missouri State energy program that has \$9.6 million in the current year, they are going to get \$60 million. A clean water State revolving fund that has \$18.8 million on an annual basis is going to get \$100 billion. And a drinking water State revolving fund that gets \$15.8 million is going to get \$30 million.

Now, the weatherization program particularly, I mean, this is—and the thing that makes me nervous about this is that I know how this is going to get covered. I am just sitting here and—everybody just circle the day on the calendar because there will be scandalous stories across the country about problems with the weatherization program. And the reason is that we are giving them so much money, and these are all going to be contracted out.

I mean, we have the St. Louis Urban League in St. Louis that typically gets a million a year. They are getting \$16 million. Now, who are they hiring? Where are these people coming from? And who is checking to make sure that there is any internal controls in this program?

So I am a little nervous that OMB has not yet come out with any guidance on the Single Audit. And I am even more nervous because I know there is a tendency—I mean, changing the Single Audit guidelines is like moving a huge tanker.

Is there anybody here from OMB?

[No response.]

OK. Well, I will make sure that we call them today.

But if they do not act quickly and say to these States, you have to make sure there are internal controls in these small, new programs, we are going to have a horrible set of stories that are going

to indict the entire stimulus, when, in fact, these are relatively small programs but with huge potential for abuse and problems as it relates to internal controls.

Tell me where you think they are in this process. I am worried. They have said they want to meet with our staff, but not until May 8. Why is this taking so long?

Mr. DODARO. I have been concerned as well. At your request, we met with the State auditors or had a conference call with them, got their ideas. We talked to the inspector general community. I thought we were moving along and making the modifications. But there is a resistance to making significant changes in the process and staying with the status quo. That is why we elevated our proposal, we had been working jointly with them on a recommendation to try to get more urgency to act.

I think it is just inertia that has prevented them from acting, and some people do not want to change the process. I think it has to be changed. I think the State auditors would use good judgment in assessing risk. Unless the internal controls are looked at for these new programs in advance of the spending for 2010, the prevention that you are talking about will just not be there.

Senator McCASKILL. It will not be there.

Mr. DODARO. And so, I would encourage you to try to encourage OMB to act on our recommendation. We think it is a reasonable approach to doing this, and I think the Single Audits can really play a big role, but only if those changes are made.

Senator McCASKILL. Part of the problem is that hardly anybody knows what a Single Audit is. Senator Carper would know, people on this Committee would know. But I think even a lot of the Members would not know. And it is just a natural. And it is just frustrating me that people do not see that now is the time to be flexible about what the Single Audit should do.

The big programs that they are going to focus on, they already have internal controls. I mean, Medicaid has internal controls. All these programs have internal controls. State highway departments have internal controls. They are used to contracting out major, multimillion dollar road projects. But this guy with a pick-up truck who is going to go out there and hammer up some weather stripping, or maybe not, and just say he is hammering up the weather stripping, and maybe he is getting his check. I mean, who is checking to see the work is actually done, especially in a program like home weatherization?

So I think it is really a problem.

Mr. DODARO. On that point, my staff just gave me a note saying OMB is now not thinking about putting the guidance out until June 30, and that is way too late.

Senator McCASKILL. That is way too late.

Mr. DODARO. Yes. So I would urge you to do that. I will continue my efforts on this as well.

Senator McCASKILL. And, Mr. Chairman, I hate to interrupt you. But I would really hope that you and the Ranking Member might consider, as the Chairman of this Committee, weighing in on this with OMB. I think it is a golden opportunity for oversight, a golden opportunity to make sure we have internal controls.

Individually, these programs seem small, compared to the overall, but if you add them all together in every State—and I think if we do not put a lot of pressure on OMB right now to tell them that they need to tweak the Single Audit requirements immediately to harness that power without spending another dime, that is a special moment in the Federal Government, when we can get real meaningful oversight without spending another dime. And we can. But if we wait another 60 days, it is going to be too late. The cow is going to be—is it the cow out of the barn or the horse out of the barn? Is it the horse out of the barn, or cow, I guess, either one?

Which is it, Senator Tester?

Senator TESTER. The hogs are out of the shed. [Laughter.]

Senator McCASKILL. The hogs are out of the shed.

It will be the hogs out of the shed that we will not be able to recapture. So I hope that I could get the added weight of the Committee leadership on this so that maybe we can convince the folks at OMB that now is not the time to rest on the way they have always done it. They really need to step up and do it differently. Thank you very much.

Chairman LIEBERMAN. Thank you, Senator McCaskill.

I mentioned before you came in that Senator Collins and I have been in communication with the Vice President's office. And he did send a letter today to us, but it bears following up on your point. But I do want to reassure you, though, to this extent.

He said that OMB is aware of some of the problems we are talking about and will begin issuing updated guidance, beyond the two they have done already, in early May. The letter says the guidance will "address several points that GAO has touched on, as well as concerns from State and local officials." And then he summarizes some of the areas of the guidance that will be forthcoming, including changes to the Single Audit precisely to ensure the Recovery Act activities receive special emphasis and audit scrutiny. But it is not clear that will be in early May.

So we will follow up to stress the Committee's concern that, specifically, with regard to those guidelines, that they will be put at the top of the list.

Senator McCASKILL. I think it is important.

Chairman LIEBERMAN. Yes. I agree. Thank you very much. Senator Tester, we do not say hogs out of the shed in Connecticut.

Senator TESTER. Well, we do not say it in Montana either, but I thought it would go over well. [Laughter.]

#### **OPENING STATEMENT OF SENATOR TESTER**

Senator TESTER. I have a very quick opening statement, and then I have some questions.

Thank you, Mr. Chairman. I appreciate you calling this hearing, and I appreciate the panel members for their good work.

The Recovery Act's transparency provisions build on efforts that I have been doing, going back to 2007, to bring more accountability and transparency to government. It is critically important. In these tough economic conditions, the Recovery Act in Montana is already working to rebuild the economy from the ground up with infrastructure projects—like roads, bridges, water systems, and many

others. But we do need aggressive oversight to make sure that these projects, with only rock solid merit, are getting the taxpayer money. So I am pleased, Mr. Chairman, with you calling this important hearing about oversight.

I have several questions, many which I had before I came in the door, and a lot more since I have been here.

I am going to start with you, Mr. Dodaro, because I have heard a lot of comments about State auditors and their role in oversight. I do not know what it is in other States, but in Montana, the State auditor's main job is insurance commissioner, oversight of the insurance industry. I do not know that they have ever been asked to do things like auditing a weatherization program, for example, as Senator McCaskill talked about.

So the question I have for you is what if—I mean, the mechanisms are there in places like the Departments of Transportation and Health and Human Services (HHS) and those kind of things, but what if the State auditor does not typically do those kind of oversights? What do you do then?

Mr. DODARO. I am not familiar with Montana, but I am with many of the States. And there is a legislative State auditor—each State is set up a little bit different. But each State has to, according to Federal law and regulations and OMB, arrange for these Single Audits. Now, some may contract them out.

Senator TESTER. OK.

Mr. DODARO. So that process is standard and in place.

Senator TESTER. Right. Quite honestly, the legislative auditor has got a full plate already in our State.

What percentage of the money can they utilize and where does that money come from to enable them to have the resources to be able to do an additional set of work?

Mr. DODARO. They are all funded a little bit differently, but I think there is some ability to recover the administrative costs of carrying out those responsibilities. But the audits are supposed to cover all spending, including the Federal spending, and then have testing on Federal compliance requirements.

Senator TESTER. Yes, but how does a legislative auditor get the money to do their audits?

Mr. DODARO. They receive an appropriation from the State legislature just like the legislature appropriates moneys.

Senator TESTER. I know that.

Mr. DODARO. Right.

Senator TESTER. The issue here is that they get their appropriation from the State legislature. The question is that they have additional work here to do. And where do they get the resources to do that? Does it come from the State legislature or does it come out of the Recovery Act?

Mr. DODARO. That is what we are asking OMB to clarify now. First, I would say, Senator, our recommendation about changing the Single Audit process would be to change the focus of it, which would not require additional money.

Senator TESTER. OK.

Mr. DODARO. But if they do not know, then OMB can determine and—



Senator TESTER. That is good. Are you recommending caps on the amount of money that they can use for audit oversight?

Mr. DODARO. We have not addressed that issue in particular, but I would expect them to use prudent judgment.

Senator TESTER. All right. Well, thank you.

There are States that have full-time legislatures and there are States that have biannual legislatures, and everything in between.

The Department of Energy (DOE) changed the rules after we went in, so the State of Montana, who happens to be in the biannual session right now, had to pull back, do some things different. That is all cool.

How do you anticipate this happening in areas where there is a citizen part-time legislature and we have OMB or anybody changing guidance, and they release it after the sessions are over with?

And this is to you, Mr. Scheppach. How do you anticipate them handling that?

Mr. SCHEPPACH. Well, again, it is going to differ quite a bit by the State. Some States, you will have to pull back the legislature for special session. Some States, essentially, have a committee that just needs to come back, and they can deal with it. Some States you could probably deal with it with executive order until the next session. So it really differs by State.

Senator TESTER. OK. A fair amount of this money is going into regions typically because unemployment rates are higher there than in other areas, where the most need is for jobs. In Montana, the Forest Service in Region 1 just gave significant moneys to the region, in the northwest part of the State. Our unemployment rate there is approaching 16 percent, very serious because of the wood products industries is in the tank.

Although there is no stipulation in the bill, to my knowledge—and I want you to enlighten me if there is—that once the money is allocated to a region, they can contract it out, and somebody from a different part of Montana or a different State could come in and do some of the restorative work, or the bridge building, or the road building, or putting in culverts and all that.

To your knowledge, is there anything in the bill that would require moneys that go to an area where unemployment is high, to actually be spent on people who live in that area that do not have jobs? Do you understand the question?

Mr. DODARO. Yes. I understand the question. I am thinking of the answer.

Basically, Senator, it will vary by program activity. Obviously, the Medicaid program is spent for the eligible population in the State, and there is a factor for unemployment rates. The highway programs have to be given priority to economically distressed areas within the counties, and they have to consider disadvantaged businesses as a certain percentage of it.

But to your particular question, I am not aware of anything that is in the legislation that would require that. I will go back and ask our attorneys to take a look at it.<sup>1</sup> But each program has its own unique regulations.

<sup>1</sup> The response from Mr. Dodaro appears in the Appendix on page 652.

Senator TESTER. I would like that, if you could do that; and then, if you have any recommendations on what I could do. Because, see, the truth is—and this is just a comment—in different regions of the country, unemployment is much higher in some areas than it is in other areas. In Montana, it easily swings 10 points.

If we are plugging money into doing important work, important infrastructure work—it is not to make work, it is work that needs to be done and should be done—but, yet, people can come in from outside to do that work, and not employ any of those people to reduce that unemployment rate, we are really not accomplishing everything that we wanted to accomplish.

So if you have any recommendations, I would love to hear them. Thanks for your work. Appreciate it.

I would like to grill all of you, or at least ask you questions, but I cannot do it. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Tester.

Maybe we will do one more question on this round.

Senator Burris, at the end, if you have more questions, I might just ask you to carry on the hearing until you are done with your questions because I want to go over to the Days of Remembrance commemoration. But let's start with one question each and see how we go. I will go first quickly, and then I will go over to you.

I am pleased to hear about how many States and localities have created Web sites to provide accountability and transparency. It really is quite remarkable. In some sense, just as the size of the stimulus is unprecedented in Federal Government history, the efforts that the Federal Government, with the Recovery.gov Web site and at the State and local level, I think are unprecedented, too, in terms of bringing modern technology to bear on all this. It strikes me that if nothing else, the Recovery Act is creating jobs for Web designers and Web managers. [Laughter.]

That is good.

But I want to ask you how the State and local sites will complement Recovery.gov, and is Recovery.gov sort of piggybacking on what the States and localities are doing, or are these basically separate sources of information?

Let's start with you, Ms. Coleman.

Ms. COLEMAN. Yes. I will give you my sense just from perusing through the various Web sites. Most of the local government Web sites I have looked at provide a link to Recovery.gov, the Federal Web site. But there is a range of content. New York City has a very sophisticated Web site and will actually be modeling its efforts to attract recovery dollars, very similar to the Baltimore City statistics local government accountability measure. So it is probably on the unique high end, but certainly New York City has different challenges and resources available.

To vary on the other end of the spectrum, there are very static Web sites are just posting the information and providing the links to not only the Recovery.gov, but also the different Federal agencies who also have all launched their own recovery Web sites. So some very dynamic ones were seen as well as some that are static, but at least making the information available and letting their constituents know who they can contact if they have questions about recovery.

Chairman LIEBERMAN. We were really impressed, surprised, by the usage, the number of hits on the Recovery.gov Web site. The last time Rob Nabors from OMB was here, it was over \$300 million since it was instituted.

Are you finding similarly heavy traffic on the State and local, or do you know?

Mr. SCHEPPACH. I do not really have a good sense.

Ms. COLEMAN. I do not have a sense of that.

Chairman LIEBERMAN. OK. How about the States' sites, Mr. Scheppach?

Mr. SCHEPPACH. Well, a lot of it is going to be duplicative. Everything that is going to go on Recovery.gov is also going to go on the States. But I think there will be more information on States about the task forces that have been created, when there are public meetings that you can attend. Also, I suspect some of them are gearing up to put out more of the regional information in terms of contracts and so on, so you can accumulate it various different ways.

Chairman LIEBERMAN. Mr. Dodaro, do you have anything to add to that?

Mr. DODARO. Yes. The only thing I would add, I know on the Recovery.gov Web site, there are links to each State Web site. So I think the links are there, which is helpful. Also, some of the States we have looked at—I know Ohio, for example, is using a Web site to take ideas from the public on specific projects. So I think some of the States are using it to get some input, too, to help them make decisions. So I would add that.

Chairman LIEBERMAN. Good. Thank you. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman. Just one final question for me.

Mr. Scheppach, I want to talk to you about the issue of the restrictions on funding being used to supplant State funding. I think this is a very confusing area because Congress put some of these restrictions into the law to ensure they were getting the stimulative effect of additional funding. If the Federal funding is simply displacing State funding that otherwise would occur, then it is not going to stimulate the economy.

On the other hand, if the funding is going to allow the States to avoid cuts that would displace people—cause them to lose their jobs or services to be reduced—then, presumably, that is a use that we want to see.

Could you help us sort through this, and do the governors have an understanding of what is supplanting versus displacement? Because as I understand it, OMB has indicated that if States “misuse” the discretionary money by displacing instead of supplementing State budgets, the Federal Government could seek to recover the money.

I think this is extraordinarily confusing.

Mr. SCHEPPACH. It is a difficult problem. And I think the biggest place that this is an issue is in the State Stabilization Fund, \$45 billion worth of education money. And the maintenance of effort there says that no State can go below their 2006 level.

The problem is that States were in such different places because we had four or five States—like Florida, Arizona and everything—that went down very early economically, and a bunch of others did

not have major problems until later. So anytime you pick a year for a maintenance of effort, it works pretty effectively for a group of States but not for others.

A perfect example there is Florida, which had, I think, cut their budgets quite significantly. So maintaining that 2006 maintenance of effort, they were so far under it, that it was causing a big problem. But at least you did build a waiver approach into it so they can apply for a waiver from the department so that it sort of helps.

It is just a difficult problem to get a concept that is effective across the board for all States. And something like the Medicaid one, where you are not measuring money, you are actually measuring eligibility and other issues, is cleaner in that sense, but in a lot of other areas, you just cannot do that.

So I think something is in there, which is pick a reasonable year for most States and provide a waiver authority is probably as good as we can do, in all honesty.

Senator COLLINS. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thank you, Senator Collins. Senator Burris.

Senator BURRIS. Ms. Coleman and Dr. Scheppach, if you could let me know what the States' position is going to be for these underserved communities, minority businesses, or the local community municipalities, whether you have any knowledge that they have in place programs to make sure that the stimulus dollars would go to minority companies, small businesses, to create jobs in those areas.

Do you have any specific knowledge as to what your municipality or the State governments are going to be doing?

Ms. COLEMAN. Senator, I would say that I do not know what all the specific cities and towns are doing. They are quite diverse and there is quite a range. But I can share that in my conversations, in our conversations with minority, local elected leaders, that they are certainly being champions for that cause as their cities and towns move forward with the requests for proposals or other decisionmaking processes as it relates to the recovery dollars.

So there are champions, hundreds and thousands of champions, for that cause who are in the local governments and a part of that decision-making process that I think will call attention to any disparities or efforts that do not seem to be in compliance with the Federal requirements, as well as any local requirements that there might be.

Senator BURRIS. Well, in Illinois, they are coming to me saying how can they get their local businesses to get a piece of this action, a piece of the project that is coming in, whether it is a weatherization project or a highway construction project. And they have no knowledge of how the process is working.

Do they talk to the mayor of the city? Do they talk to the governor of the State? And they are coming to me saying who do we talk to.

Ms. COLEMAN. Well, I would echo what you are saying in that the first step is education and awareness about what are the opportunities and how to access those opportunities. And this is where we will go back to the communication that local governments are doing with their constituents, and the vendors who are interested in these opportunities, as well as the communications from the

State and the Federal Government. These are important so that people and vendors wanting to do business can understand what are the opportunities and who do I talk to about those opportunities.

I know that cities and towns across the country, as well as the States and the Federal Government, are working hard to make those communication vehicles available so that the information is accessible.

Senator BURRIS. Do you have an example of any entity that you know about that might be an example of what is taking place? Is there a city councilman who has his business person put a grant in, let's say, for one of these community health centers, and that grant was approved?

Ms. COLEMAN. I do not have any particular examples, but I am happy to do some work on that issue when I return to the office, and we will be happy to follow up with your office.

Senator BURRIS. Will you be following that piece of it with your authority under the National Governors Association, how they are following up with the minority piece?

Mr. SCHEPPACH. It is probably not something we would normally do. The State of Illinois has appointed people who are their leads for this. And I would recommend that the community sit down with those leads and talk about this issue. I mean, no money has been spent yet—

Senator BURRIS. He is named the stimulus czar. We have a stimulus czar.

Mr. SCHEPPACH. Well, I would encourage you to sit down with that person and talk about the issue, because, as I say, you are in front of it. There are very few decisions that have been made so far.

Senator BURRIS. But right now I am getting all the heat from it. I was getting calls in yesterday about how do we get a piece of the stimulus? I mean, that is all I am hearing from my constituents. And I am now trying to get some answers from them. I have certainly met with some local officials, and they did not know as much as I knew in Illinois.

So there is major concern. And I tell you, if these dollars come into the community, and none of them get into those underserved and minority communities, then there is going to be—here again, this is what we are looking at; it is all at the top. They are going to keep us at the bottom and not give an opportunity for a chance to grow businesses and to share in our dispersion of tax dollars.

Mr. SCHEPPACH. Well, again, I would sit down with the mayors in your particular area, as well as the governor's people.

Senator BURRIS. Thank you, Members of the Committee. I appreciate your response.

Chairman LIEBERMAN. Thanks, Senator Burris.

Thanks to the three witnesses. I think this has been a very informative hearing. That is why we are going to keep doing them. And bottom line, I am encouraged by what you have all said. I think the Federal, State, and local governments are trying to work very hard together. In our oversight, there are questions, but there are responses coming, including the Vice President's announcement of the guidelines today.

Overall, the money has gone out. So not only am I encouraged about what we have heard in the short term, but I am encouraged by Dr. Ray Scheppach's vision of what history holds. [Laughter.]

We do not normally look that far ahead.

Anyway, the record of the hearing will stay open for 15 days for any additional questions or statements. I thank you all very much for what you have been doing. We had a very good turnout today, and, frankly, beyond what I expected for Members of the Committee, which shows how much interest there is among the Members. And a lot of it is because there is so much interest, as Members have indicated, back home.

Senator Collins, do you want to add anything?

Senator COLLINS. I do not.

Chairman LIEBERMAN. Thank you very much. The hearing is adjourned.

[Whereupon, at 10:55 a.m., the Committee was adjourned.]

**FOLLOW THE MONEY: AN UPDATE ON  
STIMULUS SPENDING, TRANSPARENCY,  
AND FRAUD PREVENTION**

**THURSDAY, SEPTEMBER 10, 2009**

U.S. SENATE,  
COMMITTEE ON HOMELAND SECURITY  
AND GOVERNMENTAL AFFAIRS,  
*Washington, DC.*

The Committee met, pursuant to notice, at 10:03 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Joseph I. Lieberman, Chairman of the Committee, presiding.

Present: Senators Lieberman, Carper, Pryor, McCaskill, Tester, Burris, Collins, Coburn, and McCain.

**OPENING STATEMENT OF CHAIRMAN LIEBERMAN**

Chairman LIEBERMAN. The hearing will come to order. Good morning and welcome to the witnesses and everyone else who is here.

This is the fifth in a series of oversight hearings that our Committee, pursuant to its oversight responsibility as the Governmental Affairs Committee, has conducted on the American Recovery and Reinvestment Act (ARRA or Recovery Act), the \$787 billion stimulus package that was enacted earlier this year to help pull our economy out of the worst recession in the living memory of most Americans.

We hold this hearing on the heels of what I would call mixed news about our economy. That is that we are still not where we want and need to be, but we seem to be making some progress. After a slight decrease in the unemployment rate in July, down a tenth of a point to 9.4 percent, the jobless rate, as we all know, went back up to 9.7 percent in August, which is the worst rate of unemployment in America in 26 years. We know that unemployment is a lagging indicator of an economic recovery, so this was not entirely unexpected.

We also know that just a few months ago, our financial sector was on the verge of collapse and the overall economy was teetering somewhere between a great recession and, at worst, a depression. Thankfully, both of those calamities have been averted. The stock market is up. Housing sales are up. And manufacturing grew last month for the first time in more than a year.

But the unemployment level now is above what many economists predicted when we passed the stimulus in February, particularly the numbers for the building construction trades, where unemploy-

ment still exceeds 17 percent in many States, including my own State of Connecticut. Perhaps that explains why, when I met with workers in the construction trades in Connecticut during August, they were having a hard time expressing any gratitude for the positive effects of the stimulus. So the danger of a jobless recovery remains all too real.

With that in mind, a lot of people, understandably, are asking if we can do more. Some have called for a second stimulus, although those calls seem to have receded. Others are asking, and I number myself among those, whether we can implement what we have already passed faster, whether we can speed up the process so that more of our citizens can feel the positive effects of the stimulus that we intended more quickly than will happen in the normal course. I, for one, hope that we can and I look forward to exploring that with the witnesses today.

This morning, overall, we are going to take a status check on what has been done so far and ask about the capabilities of all levels of government, and the performance of all levels of government in administering Recovery Act programs. The pace of spending naturally will pick up—we have known all along that we would spend more in fiscal year 2010 than in fiscal year 2009—and, of course, we will ask whether we can increase the pace of that spending even more.

Personally, I believe that much has been accomplished since the Recovery Act was passed as a result of the Recovery Act. While I am going to not fall to the temptation about telling old jokes about economists never reaching a similar conclusion, I think, from what I have read, most of them agree that the Recovery Act has helped halt America's economic slide and is helping the private sector toward a recovery.

I can tell you that certainly mayors and governors, and other local officials, make clear to me and others that things that would have been worse without the help that the Recovery Act provided. Let me briefly sum up where we are now and the progress we have made.

On the tax side, 95 percent of working Americans have seen their paychecks increase because of the Make Work Pay tax credit. It has put about \$23.2 billion into the pockets of these families so far. And in total since the Act was adopted, \$62.5 billion has been pumped into the economy through tax relief, with \$225.5 billion more of tax cuts still to come. Nearly 334,000 new homeowners have claimed the Recovery Act's \$8,000 first-time homebuyer tax credit. Many analysts, and maybe in some senses more importantly, many people in the real estate business—brokers, agents, etc.—that I have talked to in Connecticut say that this provision really has played a part in steadying the housing market and even now is helping to increase home sales for 4 months in a row.

In transportation infrastructure, over 6,700 highway projects have been approved and more than 2,200 are underway. Hundreds of airports across the country have been awarded funds for improvements, and about \$1.1 billion in Amtrak improvements are on the way.

The Recovery Act is also helping families through these tough times with extended unemployment insurance, increased Social Se-



curity payments, more food stamp assistance, and aid to States through increased Medicaid grants.

Recovery Act payments to the States through the Federal Medical Assistance Percentages (FMAP) program and the State Fiscal Stabilization Fund have helped, by the numbers that I have seen, keep 135,000 teachers and 5,000 law enforcement officers on the job.

We will come back to all that with some questions and answers.

Besides the spending of stimulus money, another topic of this hearing will be our continuing interest in the transparency of Recovery Act spending and a final, but critical, question that we want to deal with today with particularly the presence of—I would like to see “Hon.” before Jon Leibowitz’s name. He worked here in the Senate many years. We always thought he was honorable, but now he has been officially declared honorable.

The challenge we want to deal with today is the Federal Government’s efforts, which he is helping to spearhead, to prevent Americans from being bilked by scam artists who fraudulently promise government money in return for credit card information. Scams directly related to the stimulus appear to be few so far, but unfortunately, tough economic times are always accompanied by people who are eager to take advantage of other people’s misery and try to exploit those who are financially strapped and desperate for cash. So we look forward to that additional and unique part of the government’s response to this recession.

So I welcome all the witnesses today. I look forward to your testimony, and I am glad to call now on our distinguished Ranking Member, Senator Collins.

#### OPENING STATEMENT OF SENATOR COLLINS

Senator COLLINS. Thank you, Mr. Chairman.

Seven months ago, the American Recovery and Reinvestment Act was signed into law. Since that time, this Committee has conducted oversight to help ensure that these funds are used as intended, to help revitalize our economy by creating needed jobs, improving roads and bridges, sustaining vital health care programs, and investing in infrastructure and science.

These funds must be disbursed quickly to meet the goal of stimulating the economy. At the same time, we must ensure that haste does not make waste or permit fraud or mismanagement. Striking the right balance between speed and caution has been a challenging task.

For example, we recently learned that the Social Security Administration erroneously sent about 10,000 stimulus checks for \$250 each to people who were either dead or incarcerated. This mistake may cost taxpayers about \$2.5 million and it could easily have been prevented. Now, instead of these funds stimulating the economy, the Social Security Administration must work to recover them and put controls in place to prevent similar errors in the future.

Today, as the Chairman has indicated, we will explore three issues that could blunt the economic recovery impact of the stimulus: The first, unnecessary delay; second, inadequate transparency; and third, outright fraud.

First, some reports indicate that stimulus funds are entering the economy too slowly, delaying the potential economic benefit. The Office of Management and Budget (OMB), however, has reported that it is on track to meet the spending targets. I am interested in exploring with our witnesses whether the spending to date has had the desired effect on the economy, whether the money is being pushed out of Washington and to the intended recipients as quickly as possible.

Second, I want to ensure that we are providing the American public with accurate and thorough data about stimulus projects around the country. Congress directed the creation of the Recovery.gov Web site to increase transparency, allowing the American people to monitor stimulus spending in their own States and to help be a watchdog and report abuses. Progress on Recovery.gov initially has been slow, however, particularly when compared to some private sector alternatives.

Third, I am concerned about the growing incidence of fraud and predatory scams that appear to be on the rise as con artists prey on citizens facing financial hardships. These crooks are smart and they are opportunistic. They exploit these tough economic times to lure Americans into scams that look and sound legitimate. They use phrases that we hear on news reports and see in the headlines, such as "stimulus grants" and "government funding" to confuse victims. They manufacture forms that have an official look to them when, in fact, the services offered are not connected in any way to any government agency or to the Recovery Act.

To appreciate the potential that these scams have to spread and grow, possibly ensnaring thousands of trusting consumers, we must recognize that the Federal stimulus program is instantly recognizable. It is part of our economic and political vocabulary. It carries so much weight and credibility that the police in Florida recently used the lure of economic stimulus checks to conduct a sting operation in which 75 people were arrested.

The Florida example demonstrates the attention-drawing power that the words "economic stimulus" can have on the American people. It is critical that we aggressively pursue scam artists who brazenly use the stimulus program as a springboard for fraudulent or other unfair activities.

I have brought to the hearing today two examples of mailings that were sent to my constituents in Maine in order to illustrate my point. The first example, sent shortly after Congress passed the Recovery Act, is misleading because it resembles an official government form. It could easily be mistaken as a legitimate government offer of help and assistance. For those of you who can see the blown-up form or have it before you, it looks very much like an Internal Revenue Service (IRS) form. It provides an identification number for the individual. It has Form Number 009-S. It has "Stimulus Act 2008." It is easily mistaken for an IRS form and looks very official.<sup>1</sup>

The second example is a letter that was sent to my constituent telling him that he is preapproved for a Consumer Debt Initiative because he may be experiencing a financial hardship. Well, most of

<sup>1</sup> The chart referenced by Senator Collins appears in the Appendix on page 661.

my constituents are experiencing financial hardships, regrettably, nowadays. The letter implies that the initiative was established under the Economic Stimulus Act of 2009. In the letter, the alleged manager of the so-called Credit Relief Division, a fictitious but realistic-sounding title, encourages the consumer to call and refer to the case number provided. It has a Washington, DC, address. It looks very legitimate.<sup>1</sup>

So I am particularly looking forward to hearing from Mr. Leibowitz today about the Federal Trade Commission's (FTC) efforts to identify, publicize, and stop stimulus scams.

I also appreciate the work that the Department of Justice has done to train more than 10,000 Federal, State, and local officials to monitor the contracting process for abuses such as collusion and bid rigging. These officials can help play an important watchdog role.

With a combination of education and enforcement, we can help prevent exploitation and stop scams. At the same time, I hope that this hearing will serve as a warning to con artists out there that our government is on the lookout. We will alert citizens. We will expose scams. And criminals will be prosecuted. Preventing fraud in the execution of stimulus funding is a key element to the ultimate success of the Recovery Act.

I appreciate the Chairman's continued scheduling of very important hearings to provide sufficient oversight in this area and I look forward to hearing the testimony of our witnesses. Thank you.

Chairman LIEBERMAN. Thank you very much, Senator Collins.

I thank the other witnesses of the hearing who are here this morning. We will go now to Robert Nabors, who is the Deputy Director of the Office of Management and Budget with special responsibility for the ARRA, the Stimulus Act. Thanks very much for being with us again.

**TESTIMONY OF HON. ROBERT L. NABORS II,<sup>2</sup> DEPUTY  
DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET**

Mr. NABORS. Good morning, Mr. Chairman. Good morning, Members of the Committee, and thank you for inviting me to testify about our progress in implementing the Recovery Act.

Today, I would like to focus on four key areas that are of particular concern to the Committee. That is the rate of Recovery Act spending, recipient reporting, job counting, and the Single Audit system.

The Recovery Act is making a difference, and the Congressional Budget Office (CBO) has noted it is one of the reasons why economic activity is expected to begin its rebound in the coming months. At the heart of this approach is an effort to accelerate the pace of spending. In previous hearings, you have asked me whether our pace of spending is on schedule. The answer is yes. The Recovery Act was designed to ramp up in 2009, have its peak impact in 2010, and lay the groundwork for further growth moving forward.

In April, when I last testified here, Federal agencies had obligated about \$54 billion. Today, nearly \$234 billion has been obli-

<sup>1</sup> The chart referenced by Senator Collins appears in the Appendix on page 662.

<sup>2</sup> The prepared statement of Mr. Nabors appears in the Appendix on page 663.

gated. When combined with more than \$66 billion in tax relief, about \$300 billion has been committed to date. Importantly, agencies have outlaid nearly \$94 billion in spending so far, up from \$12 billion in April. Combined with the tax relief, this totals to about \$159 billion. This pace of spending is consistent with our original goal of outlaying 70 percent of the \$787 billion contained in the Recovery Act by the end of fiscal year 2010, and it is also consistent with CBO's initial projections.

The Administration has worked to meet or exceed a series of ambitious funding targets. As the Government Accountability Office (GAO) has noted, Recovery Act funds are actually moving to States faster than anticipated and certain programs are being implemented faster than anticipated. For example, the Making Work Pay tax credit for middle-class families was implemented about 3 months ahead of schedule, and all States obligated at least half of their highway funds at least 10 days before the deadline set in the Recovery Act.

At the beginning of the summer, the Vice President presented the Road Map to Recovery, a plan for 10 major benchmarks that would help define the Recovery Act during its second 100 days and speed implementation. Last week, the Vice President announced that the government had met or surpassed each target.

In addition to implementing the Recovery Act quickly, it is critical that we do so in a way that is transparent and accountable to the American people. That is why Congress required funding recipients to provide detailed reports on the use of funds and on the jobs that these funds have created or saved.

The first report from recipients are due on October 10. We have taken several actions in recent months to anticipate the needs of recipients and develop the appropriate leadership structure and technical capacity to manage the expected workload. Three rounds of OMB recipient reporting guidance have clarified the expectations on grant recipients and contractors. Our guidance responds to the President's charge for greater transparency by going beyond the data elements required by law to capture significant payments to vendors, those dealers, distributors, merchants, and other providers of goods and services necessary to conduct Federal programs.

Working with the Recovery Accountability and Transparency Board, we have provided detailed instructions for registering and submitting information at [Federalreporting.gov](http://Federalreporting.gov). We have worked with the board to test and fine-tune the site, which is now open for registration. As of last evening, there were about 19,000 registrants so far and we are pushing hard to increase registration.

In addition, we have worked with the board to conduct seven Webinars, attracting more than 17,000 registrants in a total of more than 20 different training sessions with recipients to explain their reporting responsibilities, to discuss how to calculate job estimates, and to review the technical solutions and data elements for reporting on recovery funds.

As some challenges will require specialized attention, we are coordinating with the board to provide on-site technical assistance in State capitals and several localities during the reporting period. We will deploy about 100 on-site liaisons to every State capital and to many of the largest counties and cities. The liaisons will provide

State and local Recovery Act coordinators with daily data on registration and reporting trends and to serve as a backstop for questions that are pending resolution from the board, service desks, and the agencies. A 10-person Project Support Team will oversee their operations, provide training, and coordinate information flow.

Finally, there will be a team of 20 to 30 coordinators drawn from different agencies, positioned to get answers from agencies and OMB to recipients and to compile reports documenting what liaisons have learned on the ground.

To further improve the flow of information, we responded to a recommendation from GAO and implemented a new State notification process, which requires agencies to notify States within 2 days of any grants awarded within their boundaries and will provide for up-to-date listings of new contracts, as well.

We are committed to strengthening the reporting processes and collecting the data that we need to track spending, count jobs, and deliver on the President's promise of unprecedented transparency and accountability.

Later today, the White House Council of Economic Advisors (CEA) will release its first quarterly macro-economic impact analysis of the Recovery Act. I am not in a position to discuss the report's specifics in this hearing, but I did want to take this opportunity to explain to the Committee the differences between the CEA report data and the data to be submitted in October by funding recipients.

The data will differ in several important ways. First, the Recovery Act recipient reports encompass only those projects and activities funded by State Fiscal Relief Grants and other investment spending. That comprises about one-third of the total spending in the Act. The CEA report, however, will assess the total Recovery Act program, from grant spending to tax relief to safety net programs.

Second, recipients are only required to report on direct jobs and not additional job impacts that may be occurring beyond that. CEA will look at direct as well as indirect economic benefits.

Finally, the October data will be driven by the quality and quantity of information provided by funding recipients. The completeness of their submissions will determine the quality of the October job count. We are working with the agencies to urge funding recipients to register and report on time and we expect the data to improve with each successive quarter of reporting. While recipient data will be useful in informing CEA on their estimating model, the two different job estimates are not intended to reconcile with one another.

As my final point today, I would like to focus on some changes that we have made in response to concerns about the Single Audit process. When I first appeared before the Committee, Senator McCaskill expressed concern that the Single Audits were not set up to meet the demands of the Recovery Act oversight. GAO echoed her concerns. Both have pointed to a few key issues, including the time lag that typically exists in the auditing cycle and the fact that the Single Audit process might not cover all Recovery Act programs that should be examined.

In response, OMB staff worked with this Committee and GAO to develop a solution that could be implemented quickly and in a targeted manner. The collaboration is ongoing. We have modified OMB Circular A-133 such that the majority of programs with Recovery Act funding will be audited. And our August 6 addendum to this supplemental stresses that auditors should be prompt in relaying any information that they discover about deficiencies or weaknesses.

Also, we are planning to use pilot authority to improve internal control communication for selected major Recovery Act programs. As part of this program, OMB will work with agencies to identify at least 10 at-risk Recovery Act programs that should be audited on an expedited basis of 6 months versus the normal 9-month time frame. To participate in the program, States must consent to being audited with respect to at least two of these programs. As an incentive, participant States will be exempt from being audited on smaller, lower-risk programs.

In addition, we have responded to concerns about State oversight capacity by issuing a memorandum that allows States to use up to 0.5 percent of funds for administrative costs and to obtain those funds more quickly than traditional schedules would have allowed.

With that being said, we continue to listen to your concerns and look forward to continuing our constructive dialogue about the critical issues over the coming weeks and months, and particularly as we approach the October 10 reporting deadline.

Thank you again for this opportunity to testify.

Chairman LIEBERMAN. Thank you, Mr. Nabors, for the opening statement. You touched on some of the items that I certainly wanted to ask you about and I look forward to the question period.

Jon Leibowitz comes to us today as Chairman of the Federal Trade Commission. We are pleased to have you with us. As you can hear from Senator Collins's opening statement and my own, we have a real concern about scam artists trying to take advantage of this stimulus program and the hard times that a lot of people are experiencing, so it is reassuring, even before I hear what you have to say, based on what I know of you, that you are on duty in this regard.

#### **TESTIMONY OF HON. JON D. LEIBOWITZ,<sup>1</sup> CHAIRMAN, FEDERAL TRADE COMMISSION**

Mr. LEIBOWITZ. Well, thank you, Senator, for those kind but perhaps undeserved words. Chairman Lieberman, Ranking Member Collins, Senator McCain, Senator Burr, Senator Tester, and Senator Coburn, I am Jon Leibowitz, Chairman of the Federal Trade Commission, and I do appreciate the opportunity to be here today.

Unlike my colleagues on this panel, who are talking about frauds directed at the Federal Government, I am going to be talking about frauds falsely invoking the Federal Government but directed at American consumers and what we do at the Federal Trade Commission to try to stop these scams.

<sup>1</sup>The prepared statement of Mr. Leibowitz with attachments appears in the Appendix on page 669.

My oral statement highlights a series of fraud cases that the Commission has recently brought involving false promises of government grants. They are part of Operation Short Change, a sweep of 120 legal actions announced on July 1 that we undertook with the Department of Justice and 14 State partners. In addition to grant scams, as you mentioned, Senator Lieberman and Senator Collins, we challenged a variety of frauds exploiting people harmed by the economic downturn. All told, with our Federal and State partners, we have brought 389 cases or legal actions in four fraud sweeps in just the past 5 months.

Mr. Chairman, to today's con artists, the challenging economy presents a golden opportunity. Sadly, it is an opportunity to prey on the economic distress of American consumers and bilk them out of their hard-earned savings. As they do with any crisis, these malefactors have sought to exploit the government's stimulus plan. Their Web sites promise government grant money, usually requiring consumers to pay in advance or to provide personal financial information. But though they promise to rescue people in troubled financial waters, after they take the money, these scammers throw consumers an anchor instead of a life line.

Some sites have even used the images of high-ranking government officials, as you can see over there,<sup>1</sup> to add legitimacy to their misrepresentations. This poster shows one site, part of the Grant Connect scam, which featured images of President Obama and Vice President Biden. Just 2 weeks ago, at the Commission's request, a U.S. District Court judge temporarily shut down these sites and we have a preliminary injunction hearing coming up tomorrow with the same judge.

But as you know better than anyone, whatever a Web site may say, the Federal Government does not award grants to individuals to pay personal expenses or bills, nor does President Obama hand out stimulus money for leisure travel.

Let me tell you about another scam, Grant Writers Institute. Grant Writers claimed that consumers could get money from the economic stimulus. Together with State attorneys general from Kansas, Minnesota, and North Carolina, earlier this summer, we filed a complaint against the defendants allegedly responsible for this scam. The defendants sent mailings, including post cards, such as the one that we blew up on this poster, "You are guaranteed a \$25,000 grant from the U.S. Government. Use your money to pay bills, start or expand a business, pay for your children's education, help you purchase or fix up your own home, travel the world."<sup>2</sup> Mr. Chairman, I am not making this up, and I know that those grants do not go for leisure travel, do they?

Chairman LIEBERMAN. No.

Mr. LEIBOWITZ. Or to individuals.

Another mailing, shown in this poster, from the same company, used—and this is very much like what you showed, Senator Collins—used official-looking seals, and as you can see, this postcard says, "Official Government Information. A \$25,000 grant from the

<sup>1</sup> The chart referenced by Mr. Leibowitz appears in the Appendix on page 684.

<sup>2</sup> The chart referenced by Mr. Leibowitz appears in the Appendix on page 683.

U.S. Government.”<sup>1</sup> Now, consumers who responded by calling a toll-free number heard this, and I am quoting again, “If you have been reading the papers, you know that recently, our government released over \$700 billion into the private sector. What you probably do not know is that there is another \$300 billion that must be given away this year to people just like you.”

Ultimately, these consumers did not get grants, but many people did fork over \$69 to the defendants and the defendants talked others into paying several thousand dollars for additional upstream so-called grant services. Just last week, several of the defendants responsible for the Grant Writers Institute scam agreed to a preliminary injunction halting their scheme.

I will briefly highlight two other FTC cases involving grants. First, Grants For You Now allegedly promised, for a fee, access to or expertise in getting free government grants to pay personal expenses. And Cash Grants Institute placed illegal robocalls to consumers advertising, “free grant money available from Federal, State, and local governments.” Its Web site included images of both President Obama and the U.S. Capitol building. Neither company, of course, facilitated grants to consumers, but both pocketed money from them. And these four cases, by the way, involve 270,000 potential victims.

We will also follow up on the poster and on the entity that you showed earlier in your opening statement.<sup>2</sup> It is conceivable that the Web site has been taken down, because a lot of the Web sites have been taken down since we announced our sweep, but we will follow up on that and get back to you.

Our actions here did not stand alone. They were part of Operation Short Change, which also challenged scams that preyed on unemployed Americans looking for work, exploited the entrepreneurial spirit of individuals looking to start their own business, promised much-needed credit to consumers, but instead delivered unnecessary debt.

As we did on this sweep, we regularly work together with State attorneys general, including those from Connecticut and Maine, and with other Federal agencies on sweeps like this, including the Departments of Justice, and Housing and Urban Development (HUD), and Treasury, and working together really can have a much bigger impact.

Mr. Chairman, we bring a lot of fraud cases, but, of course, we would vastly prefer that no one falls for these scams in the first place. One part of that solution is to educate consumers, and we do that, we think, very well, as we hope the materials in front of you demonstrate.

The Commission has also reached out to legitimate companies for help in pulling down ads for these scams. At our request, several major online ad companies, including Facebook and Google, moved to screen out ads touting the economic stimulus as providing grants for individual consumers. Let me commend these companies for their help.

<sup>1</sup> The chart referenced by Mr. Leibowitz appears in the Appendix on page 685.

<sup>2</sup> The charts referenced by Senator Collins appear in the Appendix on page 661–662.



Let me also commend this Committee for all of your support. There is a lot more to be done in this area, and we do have some ideas about ways you can make us more effective, for example, by growing our agency, which is actually about 35 percent smaller than it was 30 years ago though the American population has grown by more than 30 percent during that time. But I am happy to report that the President has committed to increasing our resources, and I am also happy to expand on this issue at my next Appropriations Committee testimony before Senator Collins. And finally, I am happy to answer any questions you have.

Thank you so much, and I will yield the balance of my time.

Chairman LIEBERMAN. Thanks very much, Mr. Leibowitz. Your statement actually justifies my confidence, as expressed earlier, and I thank you for it.

Next, we are going to hear from Earl Devaney. Are you still Inspector General at the Interior Department or are you on leave to do this job?

Mr. DEVANEY. I am on a leave of absence.

Chairman LIEBERMAN. This is a full-time job.

Mr. DEVANEY. It is.

Chairman LIEBERMAN. Today, Mr. Devaney, who has really done great public service, comes before us as Chairman of the Recovery Accountability and Transparency Board, which was created by the Stimulus Act. We look forward to your testimony now.

**TESTIMONY OF HON. EARL E. DEVANEY,<sup>1</sup> CHAIRMAN,  
RECOVERY ACCOUNTABILITY AND TRANSPARENCY BOARD**

Mr. DEVANEY. Mr. Chairman, Ranking Member Collins, and Members of the Committee, I want to thank you for the opportunity to appear before you today to provide an update on the recent and planned activities of the Recovery Board. My testimony today will address the current status and future direction of the board's missions, and after my opening remarks, I will be glad to answer any questions you have.

I would like to begin by addressing some of the suggestions put forward by Members of this Committee when I last testified before you in April. One recommendation was that the board seek the assistance of AARP and Triad in publicizing and creating awareness of recovery-related scams, like the Chairman just spoke about, given that perpetrators of scams frequently target senior populations. The board has since reached out to both of these organizations, as well as the FTC and the National Association of Attorneys Generals. And although we have seen a decline in recovery scams since the initial period of the law's enactment, the board's relationships with these groups are now in place in the event that these scams begin to rise again.

Another suggestion made at the April hearing was that the board consider employing former journalists to assist with our reporting requirements and to make the board's Web site more reader-friendly. Since that hearing, the board has hired former journalists in various staff positions, where their superior writing skills will be put to good use.

<sup>1</sup> The prepared statement of Mr. Devaney appears in the Appendix on page 686.

I am pleased to report that the redesign of Recovery.gov has been completed and its companion data collection Web site, Federal-reporting.gov, has been created, performance tested, and open for registration. As mentioned earlier, more than 19,000 recipients as of last night have registered since the site was launched on August 17. However, we are actively encouraging recipients to register prior to October 1, which is when the system will first be open for reporting purposes.

The fully enhanced version of Recovery.gov is scheduled for release prior to October 10. It will provide visitors with a visually pleasing, user friendly, and highly interactive Web site. For instance, it will have a mapping capacity that will allow visitors to search for spending all the way down to their own zip codes or their own Congressional districts, for that matter. The redesigned Recovery.gov is currently undergoing user testing by citizen groups and various stakeholders around the country.

As you may sense, I am very hopeful about the new features of Recovery.gov 2.0 and the data the Web site will display once the reporting begins next month. However, I do not believe that just throwing data up on a Web site classifies it as transparency, nor am I under the illusion that the first quarter or even the first several quarters of reporting will be free of data quality problems. This kind of data reporting represents new territory and brings the potential for new complications. The government has never before required recipients of Federal funds to report to this degree.

While I am on the subject of data quality, Mr. Chairman, I think a distinction needs to be made between data quality and data integrity. Although the board and the inspectors general (IGs) will play a role in data quality, chiefly by reviewing the agency's processes for ensuring the quality of the data, the board's main goal will be one of data integrity. That is, the board will strive to ensure that the data on Recovery.gov is a true reflection of what recipients report, including any subsequent modifications made to that data. The board intends to carefully track all changes to the data and make that information on Recovery.gov for all to see.

The prime responsibility for data quality, however, rests with the recipients of the funds and the agencies distributing those funds, as they are in the best position to know the details associated with these funds. Indeed, any direct involvement by IGs in the assessing of the data quality process could run afoul in participating in the data quality process and could run afoul of the Inspector General Act's longstanding prohibition on IGs performing programmatic functions of a department or agency, as well as government auditing standards.

Although the status of Recovery.gov receives most of the public's attention, transparency is only part of the board's mission, as you well know. The board continues to focus equally on the second mission of accountability and the attendant goal of minimizing fraud and waste.

At this point, I would like to expand briefly on my view of waste in the context of the board's mandate. Whenever I say that the board is trying to minimize waste, I am referring to an objective assessment of contracting practices rather than a subjective viewpoint of the nature of a particular expenditure or project. My view

is that aside from being mindful of the Recovery Act's flat-out prohibition on funding for aquariums, zoos, and the like, the purpose of the board is not to weigh in on spending choices that come down to an agency's judgment or opinion. Such decisions are the result of political and policy determinations made by multiple layers of watchful individuals. Instead, when the board focuses on waste in the spending of recovery funds, we will be looking principally at the incurring of unnecessary costs due to ineffective practices or internal controls.

The board continues to strategize ways to not only receive reports of fraud, waste, and mismanagement and then refer them to the appropriate IG, but also on how to analyze trends in light of publicly available open-source data. To that end, the board has recently put out a solicitation for analytical tools and personnel that can best extract and harness existing information in order to make the board's referrals more value-added for the IGs and also contribute greatly to risk-based predictions about potential fraud. We have high hopes that this risk-based fraud prevention and detection program will serve as a future model for government oversight.

The board's compliance and investigative staff also continues to review Recovery Fund procurements as they occur, coordinating with IG offices on a myriad of issues. Thus far, we have referred more than 100 matters to various IGs to ensure a heightened scrutiny of specific procurements that the board staff have identified as potentially problematic. These issues range from instance of administrative oversight to awards that may raise more serious questions requiring resolution.

The board also will be implementing a hotline where the public can report potential cases of fraud, waste, and mismanagement. After researching several public and private hotline options, the board has selected a hotline that will allow citizens to call, e-mail, fax, or mail letters to trained operators, and the board staff will then use this information to refer complaints to the relevant IGs for investigation or for other suitable response. This enhanced hotline solution will be launched in conjunction with the upgraded Recovery.gov in early October.

In conclusion, Mr. Chairman, I look forward to returning to this Committee once we have begun to unveil to the American public the full scope of recovery spending. These will be interesting times. I do not claim to be a prognosticator, but I suspect that there will be a strong reaction when the American public sees how the government actually spends its money for the first time. Some of the instantaneous reaction may be negative, but I think there will be substantial positive reaction, as well.

Whatever the short-term effects, however, I truly believe that the long-term effects of such transparency will be decidedly positive. That is why I remain optimistic that the board and I will be able to achieve success in this grand experiment created by the Recovery Act and I firmly believe that what we accomplish here will lay the groundwork for how future government spending takes place.

Mr. Chairman and Members of the Committee, that concludes my oral remarks and I stand ready to answer any questions.

Chairman LIEBERMAN. Thanks very much, Mr. Devaney.

I have a quick informational question. I remember at earlier hearings, I was impressed by the number of hits on the Recovery.gov site. Are there any current numbers on that?

Mr. DEVANEY. Well, it has gone down a little since the last time I talked to you. I think people are waiting, and I certainly am, for the new site—

Chairman LIEBERMAN. Right.

Mr. DEVANEY [continuing]. And so I am going to suggest to you that when that new site goes up, there will be a phenomenal amount of hits.

Senator MCCAIN. What potentially—

Chairman LIEBERMAN. Senator McCain wants to know, what are the numbers now, do you know? Mr. Nabors, do you have a quick answer to that?

Mr. NABORS. I do not.

Chairman LIEBERMAN. OK.

Mr. DEVANEY. I think they were about 32,000 hits per minute not too long ago.

Chairman LIEBERMAN. Yes, which is down from what it was originally. But it is still substantial.

Mr. DEVANEY. It is still substantial, and a hit does not necessarily mean that somebody comes in and spends time there.

Chairman LIEBERMAN. Right.

Mr. DEVANEY. So, quite frankly, the more appropriate measurement is how long they stay and how often they come back. So those are the kind of metrics we are going to use when the new site goes up.

Chairman LIEBERMAN. And again, the new site going up is October—

Mr. DEVANEY. Well, probably the first part of October, maybe October 5.

Chairman LIEBERMAN. So as soon as you have data on the hits, it would really help us to know those, comparatively. After it has some time to get started, I think the Committee would be interested in that.

Mr. DEVANEY. Absolutely.

Chairman LIEBERMAN. Thank you.

Our final witness is Chris Mihm, who is the Managing Director for Strategic Issues at the Government Accountability Office. Thanks for being here.

**TESTIMONY OF J. CHRISTOPHER MIHM,<sup>1</sup> MANAGING DIRECTOR, STRATEGIC ISSUES, U.S. GOVERNMENT ACCOUNTABILITY OFFICE**

Mr. MIHM. Well, thank you, Mr. Chairman and Senator Collins, Members of the Committee. It is indeed a great honor to be here today to discuss our July report on the Recovery Act. As the Act specifies several roles for GAO, including conducting bi-monthly reviews of selected States' and localities' uses of funds.

I should mention that the GAO has made a significant commitment to its Recovery Act work and I would be remiss if I did not acknowledge and express my great appreciation for the extraor-

<sup>1</sup> The prepared statement of Mr. Mihm appears in the Appendix on page 691.

dinary effort that my colleagues across GAO—we fanned out all across the country to make sure that we are providing the work that can support congressional oversight, and they have done just a remarkable job.

Our July report, the second in response to the Act's mandate, addressed, first, the uses of funds; second, the approaches taken by States and localities to ensure accountability; and third, States' plans to evaluate the impact of Recovery Act funds they receive. The report has our findings, makes recommendations, and discusses the status of actions in response to the recommendations we made in our April report. Our third report will be out later this month, towards the end of September.

As in States across the country, the budget situation is bad, and in many cases, the future looks even bleaker, and that is, in a sense, the good news. The States are being forced to take dramatic actions to balance their budgets, including staff layoffs, furloughs, and program cuts. However, and consistent with the purposes of the Act, the Recovery Act is helping States stabilize their budgets and minimize the reductions and the painful cuts that they have to take in services and minimize the need for tax increases. Many States reported to us that they would have had to make further deep cuts in services and programs without the receipt of Recovery Act funds. However, while the funds have helped cushion the impact of States' budgets, the current revenue estimates indicate that additional State actions will be needed—cuts will be needed in the coming years.

Nonetheless, significant Recovery Act funds are moving out to States and localities. Overall, across the United States as of August 28, the most recent data that we have, Treasury has outlaid about \$45 billion of the estimated \$49 billion in Recovery Act funds projected for use in States and localities in fiscal year 2009. I should mention, or just to underscore, these funds to States and localities are just a subset of the overall expenditures going out this year that you, Mr. Chairman, talked about and Mr. Nabors talked about, which include obviously the tax provisions and direct payments to individuals, as well as others. Nonetheless, this \$45 billion is a sizeable amount of money.

More than three-quarters of the Federal outlays have been provided by increasing Medicaid's FMAP and the Department of Education's State Fiscal Stabilization Fund. In addition, as of September 1, the Department of Transportation (DOT) had obligated about \$18 billion for almost 7,000 highway, infrastructure, and other eligible projects. DOT has reimbursed States about \$1.4 billion to pay for these 7,000 projects. Across the Nation, almost half of the obligations have been for pavement improvement projects, half of the highway obligations.

In regards to accountability, we reported in July that the Single Audit reporting deadline does not provide audit results in time to address identified problems and did not effectively respond to Recovery Act risks. We also noted that State auditors needed additional flexibility in funding to undertake their added Single Audit Act responsibilities. Fortunately, since our July report, as Mr. Nabors noted, OMB has moved out on a pilot program that is to have auditors provide early notice of internal control deficiencies.

If properly scoped to achieve sufficient coverage of Recovery Act programs, we believe the pilot program would largely address concerns about the timeliness of Single Audit Act reporting.

The success of the pilot program, in our view, is also very important to striking the right balance, as Senator Collins was talking about, between accountability and getting the money out quickly. If we can have these internal control reviews come out earlier rather than waiting until the full Single Audit Acts are done, then we can provide ourselves with assurance that the right controls are in place as we are seeking to get money out more quickly into the economy.

We continue to believe that Congress should provide a mechanism to help fund the additional Single Audit costs and efforts of Recovery Act auditing, and I want to express my appreciation to the leadership that this Committee has shown over the legislation that Congress is now considering in that regard.

As Mr. Devaney and Mr. Nabors noted, the next big challenge for the Recovery Act will be recipient reporting. Direct recipients of Recovery Act funds, including States and localities, are expected to report quarterly on the number of measures, including the use of funds and estimates of the numbers of jobs created and retained. The first of these reports is due, of course, in October.

OMB issued implementing guidance for recipient reporting in June that established requirements and a central reporting framework. And in recent weeks, Federal agencies have issued their own guidance and training that builds on OMB's guidance, and OMB has provided, as Mr. Nabors noted, additional clarifications on Recovery Act reporting.

OMB is also preparing to deploy the Regional Federal Liaisons that were noted to provide the on-site assistance and to establish a call center for entities that do not have an on-site liaison. These efforts, in our view, are both welcome and sorely needed.

Nonetheless, I agree with Mr. Devaney when he mentioned that indications are that recipient reporting, especially for this first round, will pose a significant challenge for many entities. As we have a mandate under the Recovery Act to comment on the jobs estimates, along with CBO that has an equivalent mandate, and will be reporting on that in November on this first round of recipient reports.

Let me conclude my comments at that point and obviously I would be happy to take any questions that you all have.

Chairman LIEBERMAN. Thanks very much, Mr. Mihm. Thank you all. It was a good beginning.

We will have 7-minute rounds of questions by the Members who are here.

Mr. Nabors, let me begin by going back to the question that I raised in my opening statement, which is acknowledging some of the positive indicators in the economy and a general view among economists that the stimulus has had a positive effect. Nonetheless, there is this stubborn persistence of high unemployment, and with that and other factors, a continuing anxiety among the American people about their and our country's economic future, which itself has a depressing effect, of course, on the economy, including on spending.

And so the question is, can we, and should we, attempt to speed up spending and, if possible, the implementation of the tax cuts to accelerate the recovery of the economy? I understand, as you said in your opening statement, that in the normal course of what was projected, we will be spending, or investing, and putting much more money in the economy under the Recovery Act in fiscal year 2010 than we have in 2009. Should we be trying to accelerate it even further to accelerate the overall recovery of the economy?

Mr. NABORS. This is an issue that the Vice President has taken a personal interest in, and he meets with the cabinet agencies once a month to go through Recovery Act issues, and first and foremost in each one of those meetings is what opportunities are available to speed up Recovery Act spending.

A couple of areas where we have made some progress. The first is an acknowledgement that there has been a lot of focus on outlays, but in certain programs, obligations have a tremendous economic benefit, as well, and that is one thing that the Federal Government has direct control over, and I will just give you an example of that.

Chairman LIEBERMAN. All right, and also give us a quick layman's definition of outlay and obligation.

Mr. NABORS. Yes, sir. What it boils down to is essentially an obligation is when the Federal Government allows a recipient to start spending money. An outlay is when the recipient actually spends the money itself.

Chairman LIEBERMAN. So it is like the authorization and then the actual check being in the account.

Mr. NABORS. Absolutely.

Chairman LIEBERMAN. Yes.

Mr. NABORS. With regard to a set of programs like transportation, for example, we have obligated a fairly large amount of money, and that money—which means that we have given the States the ability to start spending that money, but the States have been relatively slow to spend it. That does not mean that it does not have an economic impact, however.

What is actually going on behind the scenes, because of the way the transportation programs are set up, is that the money can be used to reimburse projects that have already started or that are already beginning. So what many States do is just knowing the fact that the money is available to them to be reimbursed later on allows them to go off and start the projects right away. And what you will oftentimes see is obligations that sit there for large periods of time and then a tremendous amount of outlays that come in at the end. In those instances, in programs like transportation, the availability of the money, the obligation has a tremendous economic benefit.

In other programs, there are more sensitive problems that we are trying to work with the agencies to try to address. For example, we are very focused on removing as many bureaucratic hurdles that exist within agencies as possible to allow the money to go out as quickly as possible. We are trying to do that in such a way as to be sensitive to the appropriate oversight that needs to be done over spending—

Chairman LIEBERMAN. Right.

Mr. NABORS [continuing]. But we are trying to remove unnecessary bureaucratic hurdles, including within OMB. Things as simple as doing concurrent review of projects has allowed us to speed projects up from taking months to perhaps taking weeks, and we are looking at every opportunity that we can to do that.

Chairman LIEBERMAN. OK.

Mr. NABORS. The second point that I just wanted to make is that we are trying to take lessons learned from particular agencies and trying to apply them across programs. For example, when the Federal Government spends money on programs that relate to tribes, there is a unique set of issues that pop up, and they pop up across different agencies. What we are trying to do is transplant the information that we are learning from particular agencies and trying to educate all of the agencies about the hurdles that they are going to run into and making sure that is taken into account when they are developing their spend plans.

Chairman LIEBERMAN. So, bottom line, based on what you have said, and the question that you have told us the Vice President is regularly asking, am I correct to conclude that the Administration feels that the more it can accelerate the spending of stimulus money in the coming fiscal year, in the coming months, the better it will be in encouraging a faster recovery?

Mr. NABORS. Yes.

Chairman LIEBERMAN. I assume, just based on common sense, that the more we accelerate the infusion of Stimulus Act funding, both spending and tax cuts, the better effect we will have on the unemployment rate. That is, it is more likely to create more jobs. Is that a fair conclusion?

Mr. NABORS. It is a fair conclusion, but it is a tricky conclusion, as well. Unemployment tends to be a lagging economic indicator. Just outlaying and obligating the funds does not mean we will have employment benefits right away. The faster we can expend money in a responsible way, the sooner the jobs will come online, and that is really what we are trying to do, spend money in a responsible way to create good, solid jobs that can benefit the economy over the long term.

Chairman LIEBERMAN. Obviously, we have put a fair amount of money out into the economy in tax cuts in this first period of months, \$65 or \$66 billion. But we still have, by the estimates that I have seen, over \$225 billion more in tax cuts under the Stimulus Act. Just give us a brief description of what those are, why that number is so high, because I think many of us were focused on the Make Work Pay reductions in the withholding tax that people have seen. What else is coming?

Mr. NABORS. I would point to two things, very briefly. The first point is that the tax relief was a 2-year tax relief and it was always thought that roughly half of the money would come out in 2009 and roughly half of the money would come out in 2010. So that is part of what you are seeing.

The other thing that you are seeing is a large chunk of the money is related to the Alternative Minimum Tax, and that comes due next year. So next year, we will see almost all of that money outlay.



Chairman LIEBERMAN. In other words, when people are paying their taxes next April——

Mr. NABORS. Yes.

Chairman LIEBERMAN. Is that what you are saying?

Mr. NABORS. Exactly.

Chairman LIEBERMAN. There will be a reduction in the taxes they would otherwise have paid——

Mr. NABORS. That is exactly right, sir.

Chairman LIEBERMAN. I do not know if you have a number off-hand, about how much——

Mr. NABORS. I do not, but I can provide that to the Committee for the record.

Chairman LIEBERMAN. Is the number that I have been given, that there is yet \$225 billion more in tax cuts to come under the recovery, sound right, or is it——

Mr. NABORS. I think that might be a little bit high. It is well over \$150 billion, though, but I would have to get you the specific number.

Chairman LIEBERMAN. Thank you very much. Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Nabors, previously, Mr. Devaney has estimated that as much as 7 percent of the Recovery Act funds may be lost to fraud and abuse. That amounts to an astonishing \$55 billion. We have seen some disturbing examples already. The Social Security Administration, as I mentioned in my opening statement, first sent out 8,000 to 10,000 checks to individuals who had died. Then 2 months later, we learned that the government also sent checks to people who were incarcerated and obviously did not qualify for them.

The GAO mentioned today the importance of internal controls to prevent these kinds of improper payments from happening in the first place. What precisely is OMB doing to ensure that internal controls are in place across the Federal Government to prevent fraud and improper payments?

Mr. NABORS. We are doing two things. With regard to the State and local governments that GAO mentioned earlier, we have increased the amount of money that is available to State and local governments to do their internal controls and checks, and two, we are setting up this pilot program that would allow more extensive and earlier review of programs and highlighting of potential issues to stop problems before they actually arise.

The second thing that we are doing, and I want to give Mr. Devaney significant credit for this, when he came on board, the thing that he had mentioned to me was that for this to work, we need to make sure that the IGs and the oversight is brought in—is part of the program discussions, that it is not all on the back end, because all you are doing then is catching people after the fact. So we are having ongoing discussions with our colleagues at the Department of Justice, FTC, Recovery Board, and with the IGs to incorporate as much as possible, both real-time lessons learned and best practice program management into the ongoing activities of the particular Federal agencies, and we are doing that on an ongoing basis.

Senator COLLINS. Mr. Mihm, are you satisfied with OMB's efforts in this area?

Mr. MIHM. They have certainly been doing a great deal, Senator Collins. There is still obviously more that all of us can be doing and should be doing in this regard.

One of the things, shortly after the Act was passed, the Acting Comptroller General did was to get together with the IG community, separately with State and local auditors, to collectively coordinate our audit responsibilities. Let us make sure we are getting the best bang collectively from the buck from the accountability community, that there is no overlap, that our efforts are coordinated. We are continuing to do that.

We also were focused on making sure that we were getting out the best practices in fraud prevention and in internal controls, down to program officials, not only at the Federal level but the State and local level, as well. And so there is this continuing concerted effort to get it out there.

Our continuing concern, is that we think that States, both in the audit and program communities in the States, need to continue to work doing the risk assessments and making sure that they have the controls in place down at the State level to effectively oversee and make sure that the funds are being properly spent.

Senator COLLINS. I think that is a very worthwhile effort, but clearly, there is something amiss when the Social Security Administration can send out nearly 10,000 checks that should not have been sent out. So I think we need to more aggressively look at the internal controls in the Federal Government as well as at the State and local levels.

Mr. Leibowitz, let me switch to my concern about consumer fraud. First, I am very pleased with the work that the FTC is doing in this area. I think it is absolutely essential. You discussed four cases that the FTC has been pursuing. Do you have any estimate at this point of the number of people who are being harmed by the scams, or could you give us an idea of the financial impact?

Mr. LEIBOWITZ. Sure. We know in these four cases alone, and obviously we have more investigations in the pipeline, it affected about 270,000 people. The amount of money that we think was at risk here or might have been lost to these scammers—of course, we will try to get it back and we are in the process of doing so—isn't that great. It is about \$30 million. But we think of this as a small part of the approach we are taking to going after scammers who are taking advantage of consumers who are feeling legitimate financial anxiety or having problems paying their mortgages.

So, for example, we did another sweep involving foreclosure rescue scams and mortgage modification scams, and we did it with attorneys general. And that one, for example, probably involves billions of dollars in potential losses overall.

In the financial stimulus area, it is a little bit of a whack-a-mole problem. When we did this announcement, we know that a bunch of Web sites—because we put them on the alert, we said we are going to make this a priority—just went down. And so that is good. But sometimes they pop up again, and so we keep on monitoring the Internet. We watch commercials. We look at our consumer database and we try to go after these malefactors as quickly as we can.

Senator COLLINS. I think a lot of the work that you are doing, while extremely worthwhile, is probably the tip of the iceberg, because what I have seen in my State is a lot of times the senior citizens who are victims——

Mr. LEIBOWITZ. Sure.

Senator COLLINS [continuing]. Are too embarrassed to go forth and try to file a complaint, or they are too concerned about where to go. They do not even know where to begin.

My last question on this round for you is, what advice would you give consumers who believe that they may have been taken advantage of? Who should they go to? Where should they turn?

Mr. LEIBOWITZ. Well, I would say the first thing is, if you think you have been taken advantage of in a scam, you ought to check your bank account records and you ought to check your credit card records. And, of course, there is a mechanism, especially in the credit card context, for consumers to challenge unfair or inappropriate charges.

Then we have a Web site, [www.ftc.gov](http://www.ftc.gov), and people can send complaints to us, and we look at that—and they go to something called Consumer Sentinel and we look at Consumer Sentinel all the time to monitor the number of complaints and we go after the worst malefactors. I think State attorneys general have also been very involved, particularly when the scams have a local dimension. And then if it involves an economic stimulus scam, one way you can tell if it's a fraud. First of all, there are no individual grants from the economic stimulus.

Second of all, there is a government Web site—it is run by the Department of Health and Human Services (HHS)—and is called [grants.gov](http://grants.gov), and if you want to check, it is worth checking on that Web site because you can find—it is an official Web site, not just an official-looking Web site, and you can confirm whether something you have read about or someone who has importuned you is legitimate or whether they are just out for your money.

Senator COLLINS. Thank you.

Chairman LIEBERMAN. Thanks, Senator Collins.

We will go now to the Senators in order of arrival. For the information of my colleagues, the list I have is in this order: Senators Tester, Burris, Coburn, McCain, McCaskill, and Pryor. Senator Tester.

#### **OPENING STATEMENT OF SENATOR TESTER**

Senator TESTER. Thank you, Mr. Chairman, and I want to thank the witnesses for being here today.

Before I get to my questions, I want to begin by saying a few words about a story that has bothered me over the last few weeks. It is the notion that when it comes to spending dollars, Recovery Act dollars, on ports of entry on our Northern Border, it is somehow not as important as ports of entry along our Southern Border.

Recently, there have been a few folks that have pointed to one port in northeastern Montana, in particular. That port is Whitetail. It is in Daniels County. It is a part of the country that is vast and open, and I mean that—very vast, very open. And some folks have asked me why the port is getting rebuilt with Recovery Act dollars even though it is not as busy as some other ports. A lot of reasons,

not the least to say that there are some asbestos issues. The port is 45 years old. A lot has changed over the last 45 years when it comes to our national security.

It was not my decision, but I will tell you it was the decision of Customs and Border Protection (CBP). But I will tell you that I have pushed CBP on the Northern Border to make it more secure. They did decide to upgrade all 23 ports along that border and those ports are owned by the CBP. The Northern Border is complicated. It is wide open and uncrowded in certain areas. It is very crowded in other areas and there are issues of water when it comes to the Great Lakes region. So we have to keep our eyes open as far as it comes to drug smugglers, for terrorists who would do harm to our country.

For me, it is an issue about making this country as safe as we possibly can, keeping illegal immigrants out and keeping drugs away from our kids and neighbors. It all starts by making our ports of entry as strong as they can be, by closing all the gaps and not pretend that the threats only exist on the Southern Border. Our borders are only as strong as its weakest link. I can give you plenty of examples of what has transpired over the last few years of drugs, potential terrorists wanting to cross.

But the fact is, is that I think this Committee needs to work and we need to work with CBP to make sure that no taxpayer dollars are wasted along the borders and that we maximize our security options along all our borders and all our ports, and I know our community would join me in that. Thank you, Mr. Chairman, for that.

For the questions, there have been many documents—the Ranking Member brought some up, you gentlemen brought some up—about people who are getting scammed, and the thought occurred to me, what is the penalty? If you catch these guys red-handed, what is the penalty?

Mr. LEIBOWITZ. Well, that is a great question, Senator Tester, and we are a civil law enforcement agency. So what we do first is try to shut down the scammers, so they cannot do further harm. Sometimes we can get redress for the injured consumers and the victims, and we try to do as much of that as we can, although sometimes money is dissipated. For the most part, we do not have fining authority, unlike, I believe, 47 State attorneys general.

Senator TESTER. Does anybody have the authority to put these folks in the clink?

Mr. LEIBOWITZ. Well, what we do is two things. One is sometimes we pair with State agencies, in part because they have fining authority. And then sometimes, with the most egregious cases, we pass them along to the Department of Justice for prosecution, and some of the worst offenders do get prosecuted and they do go to jail.

Senator TESTER. It just occurs to me, I mean, I was out in Montana and was harvesting when I went back for the August recess and there were ads continually about how you could personally benefit from Recovery Act dollars—

Mr. LEIBOWITZ. Right.

Senator TESTER [continuing]. In this bailout era, is what they called it. It was baloney. I knew it was baloney. But the fact is,

these guys are reaching out to people through various media. You guys talked about the Internet. They are doing it on the radio. And I think if there is no penalty, what the heck——

Mr. LEIBOWITZ. Well, we agree with you——

Senator TESTER [continuing]. If you are of that ilk.

Mr. LEIBOWITZ. Well, we support in our reauthorization, and I think as part of the Consumer Financial Protection Agency proposal by the President and Treasury, we support civil fining authority because we think that makes—or the majority of the Commission does, because we think that is important, to have a sanction.

Senator TESTER. I actually support jail time.

Mr. LEIBOWITZ. And we will not have the ability to give jail time to these people, but we certainly support——

Senator TESTER. Maybe, Mr. Chairman, we need to visit about opportunities—and I mean that in a very negative sense—to make these folks think about what they are doing.

Chairman LIEBERMAN. Yes, I think you are onto something, Senator Tester. There is obviously no better deterrent than to convict somebody who has been a scam artist and put them in jail for a while. That sends a message. And the fact that we are all seeing these ads in various media means that people are making money on the scams.

Senator TESTER. Yes, they are making some bucks.

Chairman LIEBERMAN. Yes.

Senator TESTER. Thank you. Mr. Nabors, just this week, I pushed your agency to get some money out to some water projects along the Northern Tier, and I appreciate your efforts in that. Of these particular water projects, some go to Indian country, but they are mainly Indian water projects. I guess the question is, for you or Mr. Mihm, since they are sovereign nations and the money goes out, you talked about local liaisons, do you have the ability to do oversight in sovereign nations, to make sure the money does get to the ground once it leaves our hands?

Mr. NABORS. Mr. Mihm, do you want to——

Mr. MIHM. I will defer to you, Mr. Nabors. [Laughter.]

Mr. NABORS. Yes, we do. I mean, our local liaisons are limited, but we do have the ability, working through the overall structure of the oversight community, both the IGs and the agencies who work very closely with the tribal governments to make sure that the money is spent the way we intended it to be spent, and to provide assistance to the tribal governments in terms of applying for the funding. There is a double-edge to that that we want to ensure is done.

Senator TESTER. Mr. Mihm.

Mr. MIHM. Yes. We have oversight, as well, although most of our efforts, Senator Tester, are focused on 16 States and the District of Columbia, which collectively give about two-thirds of the money and two-thirds of the population.

Senator TESTER. And we appreciate that.

I just want to talk about contracting just for a second. From what I found out, there are a lot of different levels of contracting. There is a national general contractor. There is potentially a regional general contractor. And there may be a bunch of contractors

in between that before you get to the guys that are actually running the shovels and doing the work.

Do you ever look at that system and make recommendations saying, you know what? Everybody is taking their 10 percent or 20 percent or whatever they take, and by the time we get down to the folks that are running the backhoes and pouring the concrete, there is not near as much left as there should be. Do you ever make recommendations saying, why is this done this way?

Mr. MIHM. Yes, we have, and to add on another complicating feature of that is you are seeing this play out in the Recovery Act—you can have Federal requirements in contracting and then, of course, once the money goes to the States and if they contract out, there are different requirements very often, including different definitions of what it means to competitively bid a contract, and so it can force an understanding of 50 different contracting regimes in States. So it is both a very tiered and a very complexly tiered approach to contracting that you see across government.

Senator TESTER. I would like your opinion on what we can do from a policy standpoint to take some of the complexity out of it. I will give you an example. There is a general contract, the contract in Afghanistan, the contract along the Northern Border, for example. They do not know anything about the Northern Border. They get a hold of the local folks to do it. Why are we not dealing with the folks that know what they are doing? And that is the question, how do we cut through that? I would appreciate any ideas you have on that.

Thank you, Mr. Chairman.

Mr. MIHM. We will get you that in short order, sir.

Chairman LIEBERMAN. Thanks, Senator Tester. Senator Burris.

#### OPENING STATEMENT OF SENATOR BURRIS

Senator BURRIS. Thank you, Mr. Chairman and Members. Really, I am impressed with everyone's testimony, so you are doing a great job and we really appreciate that.

Mr. Nabors, we have a bill that has been in this Committee and we have been trying to get it out. It has been held up somewhere, called S. 1064, which would give 0.5 percent of financing to those local State auditors and finance officers. You said that you are giving money to state and local governments for that increased responsibility. Is there a dollar amount that you have on that?

Mr. NABORS. We allow up to 0.5 percent to be used for administrative costs and for oversight. I think what S. 1064 does is allow an additional 0.5 percent to be used—

Senator BURRIS. Yes.

Mr. NABORS [continuing]. And we have indicated our strong support for that bill.

Senator BURRIS. Mr. Chairman, that bill has been held up somewhere and we have to get that bill to the floor. The House, I think, has already passed it. And those local governments—being a former State comptroller and former State finance officer—we need those funds. They need them and we do not want to come up short in that regard.

Mr. Leibowitz, on the consumer fraud problem, probably a response to my colleague, Senator Tester—being a former attorney

general of my State—what we have on the fraud officer is whether we are dealing with the consumer who is being defrauded out of their funds. These are not really Federal funds that they are using. They are using the vehicle of the Federal Government to defraud the consumer, so they are more of a local prosecutory responsibility there. Am I correct in that?

Mr. LEIBOWITZ. Yes. I mean, that is exactly what we do, we do a lot of education on the front end to try to prevent consumers from being victims. But yes, I think almost all of what we do involves, at least in the stimulus scam context, people who are falsely representing themselves as facilitating individual stimulus grants to consumers. But it is not entirely local in the sense that a lot of this is Internet-related, and so it has a national scope.

Senator BURRIS. But sometimes they would try to skim some stimulus money themselves. I mean, certainly the stimulus money is subject to be a victim of fraud, as well. But what you see in terms of mostly the senior citizens—is they have advertised, send us some money so that you can get your stimulus money. That is more of a local issue with the State attorneys general—

Mr. LEIBOWITZ. That is right, and that is why we work with State agencies.

Senator BURRIS. Congratulations. Please work with my former colleagues. The attorneys general are really taking—

Mr. LEIBOWITZ. The attorneys general are terrific. They are on the case in this area—

Senator BURRIS. And also our State auditors, as well. They will do a tremendous—

Mr. LEIBOWITZ. And just going back to your point and Senator Tester's point, a lot of the cases we are bringing are really criminal fraud cases, and so we are prosecuting them because this is in our bailiwick, but they could also be prosecuted criminally.

Senator BURRIS. The Federal Government is letting out contracts with contracting agencies to help track these funds or to bring in computer skill teams to help them with all of this, and I want to know how much of these stimulus dollars that are coming directly into costs that are going to minority contractors. And for some reason, we find it difficult to get this kind of data. With the stimulus money, there are outside contracts that are being let in order to process this, and if you have any information on that, Mr. Nabors, in terms of how we are handling that for minority contractors, and specifically if you have any black contractors.

Mr. NABORS. I do not have the numbers specifically for black contractors, but some of the more recent numbers that we have with regard to some of our small business targets, small businesses have received about 22 percent of the contracting dollars—

Senator BURRIS. Now, are you talking about small minority businesses?

Mr. NABORS. No. I am going to go through a list of numbers for you. Twenty-two percent for small businesses. About 3 percent for disabled veterans businesses. And about 5.9 percent for Historically Underutilized Business Zone contractors, which in some ways captures some of the minority businesses. I do not have a specific number for you for black businesses, but I will see if I can get that number for you.

Senator BURRIS. Would you please, and Hispanics, as well. Hispanic and black businesses. There is deep concern about making sure that there are skills in these areas and that our government is being aggressive in supporting those type of businesses for their economic viability.<sup>1</sup>

And I did have another question, but I got so wrapped up in that one. Mr. Leibowitz, in terms of the numbers, you gave Senator Collins the numbers of the frauds. What was it, 270,000 people and \$30 million—

Mr. LEIBOWITZ. For these four cases that we brought along. We know that there is more fraud out there involving the stimulus, but in the cases we brought thus far, that is our estimate of the number of consumers harmed and the amount of the potential harm.

Some of these schemes involve initial payments on a credit card of, say, \$1.99 or \$2.99, but then there is what we call a negative option scam that is part of this, where they have your credit card number. They just keep on billing you every month, and until you figure out that you can cancel it, and if you cancel it in a timely manner, then you keep on paying. As someone in a different context who has been a victim of a negative option scam, they are sometimes hard for the individual consumers to detect.

But again, we also know that there are more people out there who are probably victims. We watch the Internet. We look at advertisements all the time. We look at our consumer database and we try to do as best we can to stop these types of frauds.

Senator BURRIS. Mr. Devaney, we are going to have a new Web site, Federalreporting.gov 2.0, or is Recovery.gov still available?

Mr. DEVANEY. Recovery.gov is up and running right now, Senator, and will be replaced by a newer version around the first part of October.

Senator BURRIS. October 10, because I just told a couple of people to go to Recovery.gov—

Mr. DEVANEY. No, you still go to Recovery.gov and you will get the newer version when we put that up.

Senator BURRIS. OK. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks very much, Senator Burris. Senator Coburn.

#### OPENING STATEMENT OF SENATOR COBURN

Senator COBURN. Thank you, Mr. Chairman, and let me personally thank each of you for your service. You have a tough job, a really tough job. What we want to be is not somebody that is critical, but really someone that is helpful.

Mr. Nabors, in your testimony, you said that each of the stimulus projects is carefully reviewed by OMB to ensure that their uses of Recovery Act funds are thoughtful and appropriate. You work with agencies to identify and revise projects that do not meet that threshold. Could you make that list of those projects that you have identified and revised available to the Committee?

<sup>1</sup> The response from Mr. Nabors appears in the Appendix on page 754.



Mr. NABORS. I do not know that there is a consolidated list of those types of activity, but let me go back to the office and see what we have and what we can provide to the Committee.<sup>1</sup>

Senator COBURN. One other concern that I have, and again, I am sure these are old numbers, but the *Government Executive* article on August 31, 2009, said that more than half the Recovery Act contracts that the Federal agencies have awarded are on a cost-plus basis. I agree with the President. That is exactly what we do not want to do. We want fixed-price contracts. We do not want cost-plus contracts. Cost-plus contracts always cost more. What is the Administration doing, Mr. Nabors, to make sure that this trend, as reported in this article, does not continue? It is 53 percent of all the contracts let so far are cost-plus, which is pretty worrisome.

Mr. NABORS. I think we are doing two things. First, the Director of OMB and the President put out instructions to the agencies that our preference, when at all possible, is to use competitive processes and to ensure that, as much as possible, that we are using fixed-price contracts. I think what we are seeing with the cost-plus is somewhat of an anomaly because a lot of that is being driven by the Department of Energy. And where we have seen a lot of variable-price contracts used is when you have things like research and development, where the true costs are not known up front.

If you look at most of the money for that category of contracts right now, about 90 percent of the money is the Department of Energy, which was not unexpected.

Senator COBURN. And that went out earlier than much of the other money—

Mr. NABORS. Exactly.

Senator COBURN [continuing]. So that tended to skew it. Well, I am willing to stand corrected on the numbers, because I know that is just a snapshot. All I am saying is I am concerned about it and I know the President is concerned about it.

The other point I would make and I have made it several times, if you do not get a buy-in of companies' capital on research, in other words, having capital at risk when they get these contracts, they are not ever going to be as efficient.

So my message to you would be, even though it is the Department of Energy and even though it is research, companies should put capital at risk. That is one of the ways we are going to control the costs. When contracts are cost-plus, managing those contracts are difficult. You are looking at after-the-fact rather than preventing it in the future. The way to get that is to make sure those contracts—those companies have to have some of their capital at risk.

Mr. NABORS. The point well taken, sir.

Senator COBURN. That will help us a lot.

Mr. Devaney, again, for you and Mr. Nabors, because I am very appreciative of your work, are we going to be on time with Recovery.gov and the Web site?

Mr. DEVANEY. Absolutely.

Senator COBURN. So it is coming up on the 10th or the 11th of October?

<sup>1</sup> The response from Mr. Nabors appears in the Appendix on page 755.

Mr. DEVANEY. It will be up before that.

Senator COBURN. One of the things that is bothering me a little bit, and I know it is a big job, but you differentiated between integrity and quality. I do not have any doubt that you are going to make sure that the integrity of the data that you are putting up is accurate, but I am wondering, can you reach further to make sure that the quality of data is accurate?

Mr. DEVANEY. Well, it is a major concern, Senator, and growing, quite frankly, that we have at the board. We are asking, as I mentioned in my oral remarks, for recipients to report far more things to the Federal Government than they ever have before, and it is a tough job. They have to meet the deadline of reporting, which is October 10, and they are doing some unique things out there. For instance, 30-plus States are going to be reporting centrally in bulk form, and I think they are doing that to ensure that they report on time and to maybe give themselves a tad more time to look at the data at the State level to ensure that it comes in in an accurate way.

But having said that, I am concerned that the public's view of inaccurate data would actually harm rather than enhance transparency. So, the board and I want to do everything possible to allow folks to go in and check that data once it has gone in, to make revisions if they have to, and we are going to track those changes very closely.

Senator COBURN. Is it going to be starred on the Web site so everybody else can see that this has been changed?

Mr. DEVANEY. We are going to be tracking and chronicling those changes on a daily basis and make all of that available for anybody who wants to see, for instance, to download it and just take it off and look at it for themselves. But also, we are going to put up on the Web site a dashboard, if you will, with pie charts and graphs that shows where the changes were made, what categories changes were made in, whether or not X-percent was over at the Department of Commerce. We are going to make all that available for everybody to see after those changes take place.

Senator COBURN. Part of your statement was the fact that you think this is going to change the way the government operates. Actually, the President, Senator Carper, myself, and Senator McCain put through USAspending.gov. Recovery.gov is modeled after USAspending.gov. If it accomplishes everything, it is going to be great, and I agree with you. But the quality of the data—the integrity can be fine, but if the data is not any good, and it is not a true reflection of what is happening, we really have not bought anything.

What is going to be in force to make sure that the agencies which are going to be responsible for the quality of data will—at least, that is what I understood you to say—

Mr. DEVANEY. Yes.

Senator COBURN [continuing]. Bring good quality data to you?

Mr. DEVANEY. Well, the agencies are going to be actively involved in looking at that data along with their State recipient counterparts to get it in the best shape possible. My suspicion is it will get better as—the second quarter will be better than the first quarter, etc.

As you may know, when USAspending.gov was stood up initially, 51 percent of the data was inaccurate——

Senator COBURN. Yes.

Mr. DEVANEY [continuing]. And we are 2½ years later and it is 13 percent, 14 percent inaccurate. So it is a hard thing for recipients to report data, seemingly, and we are asking them in this instance to report more data than they ever have before. So it is going to take a leveraging of resources. OMB is going to play a role. The agencies are going to play a role. And I can assure you the Recovery Board will do its best to aid in that process.

Senator COBURN. All right. You are having a problem with quality right now, is that correct?

Mr. DEVANEY. Right.

Senator COBURN. So the site will be up, but full implementation of the site probably is going to be some time, is that correct?

Mr. DEVANEY. Well, the site will be up and very interactive. As I mentioned earlier, you are going to be able to do a lot of things and slice and dice the data any number of ways you want. And our hope is that the data will be as accurate as it possibly can be, knowing it will not be fully accurate initially, and that it will get better. I really do believe that once people get used to doing this, this being the first time and coming at an awkward time of year—October is usually an awkward time for most financial entities, particularly in the States—we will have a lot of good data in there after a period of time.

Senator COBURN. Thank you very much.

Chairman LIEBERMAN. Thanks very much, Senator Coburn. Senator McCain.

#### OPENING STATEMENT OF SENATOR MCCAIN

Senator MCCAIN. Thank you, Mr. Chairman, and I thank the witnesses for being here today and all of their hard work.

Mr. Mihm, in March, the GAO launched a hotline Web site for citizens to report waste, fraud, or abuse. How many complaints has that hotline received?

Mr. MIHM. Senator, we have 80 credible or initially credible responses that came in. Of those 80, we are doing eight detailed investigations. From those, another 12 or so are pending, and then 22 of them we have referred over to the inspectors general. I do not have the top-line number of how many have come in, but at least 80 of them were credible enough to warrant an additional review.

Senator MCCAIN. So it has been worthwhile?

Mr. MIHM. Yes, sir.

Senator MCCAIN. Thank you. I noticed in your prepared statement, Mr. Mihm, that one of the charts,<sup>1</sup> Figure 2, Estimated Federal Recovery Act Outlays to States and Localities, in 2009 as a share of the total, and then it goes on to show 87 percent of estimated Federal Recovery Act outlays to States will be in the nine programs that you have reviewed.

Mr. MIHM. Yes, sir.

Senator MCCAIN. Sixty-three percent has been in Medicaid?

<sup>1</sup> The chart referenced by Senator McCain appears in the Appendix on page 699.

Mr. MIHM. Yes, sir. That is the adjustment. The increase in the FMAP was a 6.2 percent across the board that went to all States in increasing the Federal match and then an additional bump-up for States that had significant increases in unemployment rates. So for the first couple of rounds, this is the big money issue that is out there. Most of the States are using it in order to maintain eligibility and deal with increasing caseloads that they are having as a result of the recession.

Senator MCCAIN. And tell me how that is a job creator.

Mr. MIHM. First, since this is a mandatory program, it does not have to be reported as part of the recipient reports in terms of job creations or job retained, and so they are off the table in that regard. What it usually does, or what many of the States told us, is in addition to helping with eligibility in caseloads, it also freed up State money, and then the State money has allowed them to do less draconian cuts than they otherwise would have done. But again, the short answer to your question, sir, is that they are not subject to the reporting requirements that we have been talking about in terms of—

Senator MCCAIN. And how much money are we talking about in this 63 percent that went for Medicaid?

Mr. MIHM. It will be \$87 billion over a 2-year period. The exact money is that it is \$19.6 billion from October 1, 2008, to September 4, 2009, in the 17 locations we have been looking at.

Senator MCCAIN. Do you have any comment on that, Mr. Nabors?

Mr. NABORS. I concur with the assessment. I think our view of the importance of the FMAP program is exactly how Mr. Mihm laid it out. What States have told us is because they have access to this FMAP money, in other areas, such as education or law enforcement, there is reduced pressure on their budget and they are able to both create and retain other types of jobs through the availability of the FMAP money.

Senator MCCAIN. Sort of a trickle-down economics, I guess.

Mr. Nabors, I have seen many Administration witnesses and I understand that you have to tout the success of whatever program that the Administration is running. I do think that it might be well to complete the record, that when the stimulus package was being considered in the U.S. Senate, the economic advisors to the President and the Director of OMB said that a maximum unemployment would be 8 percent. It is now 9.7 percent.

I just came back from spending a lot of time in my State, as many Members did, and my State is one of the hardest hit, and our small business owners that are closing their doors and storefronts and shutting down are asking me why they are too small to save and financial institutions are too big to fail. I have yet to come up with a very good response to that.

So the fact that unemployment is at 9 percent, lag or not lag, comes as small comfort to the citizens of my State who are unemployed and the people who are unable to remain in their homes with one of the highest foreclosure rates in the country. I would be glad to hear your response to that diatribe. [Laughter.]

Mr. NABORS. Sir, I do not disagree with anything that you have just said. Our initial assessments of the state of the economy was

based on inaccurate and incomplete information and the downturn in the economy turned out to be much more significant, much more severe than we had originally projected in January and February. As we look at the unemployment growth—and it is not just the numbers that we are seeing today, but the numbers that we put out in our mid-session review project that unemployment could reach as high as 10 percent. That is unacceptable to us. As I said to the Chairman and to the Ranking Member, we are trying very hard, as much as possible, to increase the spending coming out of the Recovery Act and to try to do everything possible to minimize the impact of this recession on the American people.

Senator MCCAIN. I thank you for that answer, Mr. Nabors.

Mr. Mihm, in your prepared statement, there was a number of recommendations that GAO had proposed. There is not a page number on it, but it says, GAO recommendations, accountability, and transparency, then you have various bullets. Have those recommendations been largely complied with, and if not, maybe for the record, you could provide us the areas where you think there needs to be further accountability and transparency.

Mr. MIHM. In the second half of your question—yes, sir, in our September report, the one that is coming out in a couple of weeks, we will give an assessment of all the recommendations we have been making and where OMB or other Federal agencies are in that regard.

Now to the first half, as to whether or not they have been complied with, as I mentioned earlier, I think the pilot program that Mr. Nabors was talking about for Single Audit is very important to addressing many of the concerns that we have in regards to the accountability and transparency aspects here, and that is that we need this internal control testing earlier. Not to get into too much of the weeds of this stuff, but most State fiscal years end on June 30. The Single Audits then come out 9 months after that. That is the required date. Often, they lag a little bit more than that.

And so we will not know how things are going from an audit perspective in States in some cases, for the fiscal year that has just begun, until March 2011. There has been too much money by that point, of Recovery Act money that will be out the door, and so then it will be just a historical document rather than a document that can really help people manage and help us to address risk. That is why we need the risk assessments to come out earlier from the State auditors, so that as a deficiency or weakness is identified, they can be dealt with before they become big crises, before they show up over at FTC, for example. So focusing on that pilot is very important to us, and I know it is a major focus of the Administration.

Senator MCCAIN. I thank you. Mr. Chairman, my time has expired. I want to thank the witnesses. Mr. Leibowitz, I am not sure we need this packet, but it is very good information. Thank you.

Chairman LIEBERMAN. Thanks again, Senator McCain, for your thoughtful questions, and, I might add, your high-quality diatribes. [Laughter.]

Senator McCaskill.

# **OPENING STATEMENT OF SENATOR MCCASKILL**

Senator MCCASKILL. I am going to try to live up to the example that Senator McCain had—

Chairman LIEBERMAN. I have every confidence that Senator McCaskill—

Senator MCCASKILL [continuing]. On diatribes. [Laughter.]

First, let me say, I could not agree more with Senator Tester. These people that are out there preying upon folks at this point in time, they are pond scum and they should go to jail, and whatever we need to do to help them go to jail, you need to let us know, because I know you are doing sweeps, I know you are doing all this, but nothing counts more than cuffing somebody.

Mr. LEIBOWITZ. I absolutely agree with you, and in the context of the Commerce Committee reauthorization that we hope to see later this year or early next year, we will have some ideas we can talk over with you.

Senator MCCASKILL. Great.

Now, I do not want you to think, Mr. Nabors, that I am picking on you, but it is going to feel like I am picking on you. We sent out requests to all the State auditors asking for input on how they think this is going in light of their Single Audit responsibilities and the stimulus funds that are out there. One of the things that came back loud and clear was the ridiculous—I think ridiculous notion that we are mechanically making the decision that any program that gets ARRA funds becomes a Type A high-risk program.

Let me give you a good example—foster care. Foster care is a low-risk Type A program under A-133 and the ARRA funding is approximately 2 percent. And what you do now is you push that into high-risk as an A-level program, which takes a tremendous amount of resources in terms of auditing. I really think you have missed the boat in terms of using the expertise on the ground of the State auditors that are doing these Single Audits to make decisions about high risk and low risk as it relates to these monies.

And I am just curious, and I do not mean to be a smart aleck, but is there anyone that is making these decisions over there that has ever done a Single Audit?

Mr. NABORS. The answer is yes, and I do not feel that you are picking on me and I will try to answer appropriately. There are people in our shop that have done Single Audits and we are in constant communication with the auditing community. In essence, the pilot program that we are proposing today was born out of conversations that we had with GAO, with some of your staff, and with the audit community. That conversation is going to be ongoing and we will continue to have that conversation with them.

Senator MCCASKILL. Now, I have to really pour lighter fluid on the charcoal briquettes here, because I have to figure out, if we are just rolling out a pilot program, do we have specifics on when this is going to—I think Mr. Mihm and Mr. Devaney will back me up—the barn door is already open and the cow is out of the barn and we are announcing the rollout of a pilot program. It will have no value whatsoever, as Mr. Mihm just said, if this pilot program isn't on the ground ASAP.

I am worried that we have gone this many months and we are announcing a pilot program. How many States are in the pilot?

How are you informing the States of the pilot? The State auditors of Missouri do not know anything about it. How long will the pilot last? How much relief from other programs is being given in connection with the pilot programs?

Mr. NABORS. The pilot program was just announced today by the Deputy Director of the Office of Management and Budget, so we will be providing additional guidance about the pilot going forward. But this is something that we plan on implementing almost immediately. We do want to make sure that we are in very tight coordination with the GAO. It is one of the things where we believe that we have made a change in the oversight regime. Too often, OMB and GAO go off on their separate ways.

Senator MCCASKILL. Right.

Mr. NABORS. In this instance, we actually sat down and tried to figure out what actually makes the most sense.

In terms of some of the specifics that we have already fleshed out, the number of States, it actually would be available to any State that wants to involve themselves in the pilot. We are calling it a pilot mainly because we are using pilot authority. That is the authority that we have available to us to make these types of determinations. But it would be as expansive as the number of States that want to participate in the program.

Our initial vision of the program is that we would look at the 10 highest-risk programs based on conversation with GAO and the agencies and say, of that list, a State that wants to participate in the pilot has to select two of those programs for expedited audits. If they want to participate in the project and they make those two selections, then what we will do is we will give them relief from doing audits on smaller, lower-risk programs.

Senator MCCASKILL. Well, that is terrific, and I am glad to hear it is going to be available to anybody who wants to participate. I am really pleased you guys are working closely with GAO. I do know you are in contact with the State auditors, but I do think if you guys will let loose of the reins a little bit as it relates to the Single Audit, knowing that next year's Single Audit is big because of the way this money is rolling out, I think you will find you will get a much better product that will provide much more transparency and accountability than just arbitrarily saying everything that gets ARRA is high risk. I think that is a huge mistake.

Mr. NABORS. Well, we do allow the auditors to ask for an exception, but I take your point for what it is—

Senator MCCASKILL. The exception is really hard. I mean, it is a big bunch of paperwork. I have asked for exceptions before. I know that it is like arm wrestling a gorilla to try to get an exception. So I think it would be better if you could figure out a way to loosen up a little bit.

Mr. Devaney probably will not like this—but I had never met Mr. Devaney until I came to Washington, but I know that he spent 20 years in the Secret Service. He was Director of Criminal Enforcement at the Environmental Protection Agency for 8 years. He has been an inspector general for 10 years in the Department of the Interior. I would say that he and the staff he directed caught Jack Abramoff and the corruption involved there.

I think to use his name on a list of cheap political hits by calling him some kind of unaccountable czar is unfair to him as a public servant. I think that the members of this body should rise up and defend people like Mr. Devaney, who have clearly not come to government to make big money, who clearly do not have political allegiance, who clearly have done everything in their career to look after the public's money. And I think including him and others on some cheap political hit list by some cable commentator does a disservice to him and many of the other people that are serving in positions of accountability and I wanted to put that on the record before I finished.

Mr. DEVANEY. Thank you very much, Senator.

Senator McCASKILL. Thank you, Mr. Chairman.

Chairman LIEBERMAN. Thanks, Senator McCaskill. I appreciate what you said and identify myself with your remarks. I want to say, from visual observation, you are right. Mr. Devaney was very uncomfortable as you were praising him. [Laughter.]

Senator Carper.

#### OPENING STATEMENT OF SENATOR CARPER

Senator CARPER. I thought he was uncomfortable at first, but I thought the more you got into it, he kind of relaxed and— [Laughter.]

So toward the end, he seemed like maybe he was enjoying it.

I was going to take a cheap shot at you, but I guess I will not. Sometimes we run into people in our business, on this side of the table, and people know we are elected officials and they will say, "Are you some politician? You are one of those politicians, aren't you?" And over time, I have taken to either saying, well, actually, I am not. I know some who are. But sometimes I will describe myself as I am just a servant. Or sometimes I will say, well, I am a statesman. [Laughter.]

I used to be a politician, but now I am a statesman. Whenever I hear folks called government bureaucrats, I do not take too kindly to that, so we thank you for your service and I, too, would like to be identified with the remarks of Senator McCaskill. That is one of the nicest things I have ever heard you say about anybody. So treasure this day. [Laughter.]

Senator Coburn is gone, but he and I share an interest in a number of things, along with others on our Committee. One of the things we have an interest in is trying to recover money that has been misappropriated or money that has been misspent. One of the laws we have to comply with deals with improper payments, and we know that every year, agencies are supposed to report their improper payments. And last year, I think OMB told us that we are up to about \$72 billion worth of improper payments, mostly overpayments, and we are offering legislation this year to not just tighten that money up, but to go after and recover more of the money that is inappropriately spent.

When folks ask me, well, how are we going to pay for health care? Where is the money going to come from, and without cutting people's benefits in ways that are untoward? I talk to them about what we are doing in going after money in the Medicare program that has been inappropriately or fraudulently spent. The last cou-



ple of years, we have been going after and trying to recover money from Medicare, a lot of it fraud.

The first year we tried to do it, we did not get anything. The second year, we just got a little money back. The third year, last year, we got \$700 million in just three States. This year, we are going after recoveries in the other 47 States. If that goes well, we hope to be able to do the same kind of thing in Medicaid.

I wanted just to ask you all to share some thoughts with us about when we find where there has been fraud, where monies have been misspent, inappropriately spent, what are we doing, or what are we prepared to do to go after and reclaim the money for the Treasury and for the taxpayers?

Mr. DEVANEY. I will take a stab at that.

Senator CARPER. Please.

Mr. DEVANEY. I think that early on, the board and all the IGs have been interacting with the Department of Justice. There is an already existing task force, Procurement and Grant Fraud Task Force, that provides entre into the 95 U.S. Attorneys' Offices around the country, and when a case comes up, we are going to be very aggressive about seeing that gets prosecuted, as aggressive as we can possibly be if the facts support those kinds of things.

So I think the answer is we have about nine cases right now that are in the various U.S. Attorneys' Offices, which is a very small amount, and quite frankly, I am a little surprised it is that small. But as soon as we see it, we make sure the appropriate IG is doing an investigation and that gets brought into a U.S. Attorney for review. And we work closely with the Department of Justice. And I know from talking to them, they are very interested in sending some very loud signals early as often as they can with this money.

Senator CARPER. Does anyone else want to respond?

Mr. LEIBOWITZ. Just from our perspective, when we see consumers as victims—and that is where our jurisdiction is—we go after it. We work with Treasury and Justice. Some cases we refer for criminal prosecution because the fraud is so egregious. And with State attorneys general who are often better equipped to get fines and then to go after malefactors who are in their jurisdiction. So we try to do this collectively.

And we also try to look at where the money is going. I mean, it is really the title of this hearing. Fraudsters or malefactors are opportunistic. They go, like Willie Sutton said, where the money is. And so you want to try to at least figure out where it is going a little bit in advance so you can get there maybe a little bit before, sometimes.

Senator CARPER. If I did not misunderstand, I think Senator McCaskill used the word “pond scum”—not a word we hear every day.

Mr. LEIBOWITZ. It is a legal term of art, actually. [Laughter.]

Senator CARPER. Probably a well-chosen word in this case, describing some of the folks who are trying to take advantage of people with some of this money that is supposed to be used for economic recovery. And I think she said there is nothing that is more effective, maybe, than cuffing somebody that has been behaving, not just badly, but criminally.

And the other thing that is really important is, as we follow the money and money that has ended up where it should not be, let us get it back. To the extent that we can get the money back, we need to do that. Find and cuff people, that is good if they ought to be cuffed. We ought to get the money back as much as we can.

The other thing I wanted to mention, our Governor in Delaware; Mike Castle, our Congressman; Ted Kaufman, our colleague; and I were down in an area between Wilmington and Dover, the other day where Senator Lieberman has driven by a time or two when he was running for President in 2004 on the campaign trail. His campaign trail came right by this place.

But we had a major expansion of, of all things, a park-and-ride, which sits right alongside two major north-south highways in Delaware and in a bedroom community place called Middletown. We were expanding the park-and-ride. We are putting in bicycle paths and pedestrian walkways from some of the neighborhoods that people can get to the park-and-ride. We are initiating new bus service for the park-and-ride. So it is actually a nice multimodal deal.

The anticipated cost of the project had been about \$900,000. The price of the project came in at \$600,000, and what I am starting to notice, and I do not know if my colleagues here are noticing it in projects in their States, we have a lot of people, a lot of contractors hungry for work and anxious to bid. I know Senator Coburn expressed concern about cost-plus contracts, but we are finding that, probably better than any time I can remember, bids coming in under—way under, in some cases—the anticipation. I do not know if others are seeing that. Mr. Mihm, any comments on that?

Mr. MIHM. Yes, Senator Carper. Your experience is consistent with what we have seen in other States. The transportation officials are telling us the bids are coming in anywhere between 5 and 30 percent below what they had originally estimated. It does show that the economy is in bad shape in the sense that they are able to get that, but it is also a good deal in that then they are able to do additional infrastructure projects or additional transportation projects because of that. And so your experience is, again, consistent with what we have seen elsewhere.

Senator CARPER. In this case, it was a Delaware Department of Transportation (DelDOT) project, but the extra \$300,000 stays in the State, can be used for other DelDOT projects, that is my understanding. Is that correct? All right. Good. Well, that is a silver lining in what can otherwise be a rather dark cloud.

Thank you very much. Thanks for your stewardship. Thank you for giving the term “government bureaucrats” a good name. Thank you.

Chairman LIEBERMAN. Thanks, Senator Carper, very much.

Senator Collins and I each have a few more questions and so we will try to do them as quickly as we can.

Mr. Nabors, in your opening statement, I would say that you veered slightly over into Mr. Leibowitz’s territory in what I would call some consumer protection, which is with regard to the report of the Council of Economic Advisors today, and I was interested in it and I appreciate it. I think what you were saying is that this first quarterly report of the Council of Economic Advisors today on the Stimulus Act will produce results that will be greater than the

recipient reports that come in in October, and I presume in job creation particularly, and this will arouse some controversy, so I appreciate your raising the point.

The temptation is to ask which one of the two will be right, or to some extent are you saying that they will both be right because they are both answering different questions?

Mr. NABORS. I am saying the latter. Really, what we are asking the recipients to tell us is how many direct jobs did you create using the Recovery Act funding. What we are asking CEA to do is to calculate the economic impact of the Recovery Act overall on the economy, and there is more than just direct jobs from direct Federal spending involved in that.

As I had mentioned in the conversation with Senator McCain, even something like FMAP is viewed as having an economic benefit, because even though it does not directly create a job, it does free up money for States to use in other areas and those areas are seen as producing jobs, either for law enforcement, education, or in other fields.

So what the CEA report will do is two major things that are different from the recipient reporting. One, it will calculate a broader base of job creation. It is not just capturing direct jobs, but it is capturing direct, indirect, and what we call induced jobs, the jobs that are created as a result of manufacturers producing things for highway companies that are building the roads. All of that will essentially have a trickle throughout the entire economy.

Chairman LIEBERMAN. Yes.

Mr. NABORS. The second thing that the CEA will be doing is when you look at the direct jobs that the recipients will be calculating, it is not necessarily clear that they have all of the information with regard to jobs that are necessarily retained as a result of that money, and that is something that is very important in the overall context of the economy, and that is something that CEA's report will also be capturing.

Chairman LIEBERMAN. Right. So I want to move on to one more question, but it sounds to me as if you are saying they are both right. They are both answering different questions. But is it correct to infer that you are also saying that the CEA answer is a more comprehensive answer—

Mr. NABORS. Absolutely.

Chairman LIEBERMAN [continuing]. And therefore, perhaps ultimately more accurate. It is not that the recipients are being inaccurate, but they are not calculating all the effects of the stimulus—

Mr. NABORS. It depends on what precise question you are asking. If you want to know how many jobs the transportation project in your neighborhood created, then the recipient reporting—

Chairman LIEBERMAN. Right.

Mr. NABORS [continuing]. Is probably more accurate. If you want to know what the economic impact of the Recovery Act and all of its manifestations are, then the CEA estimate is going to be more accurate.

Chairman LIEBERMAN. That is actually a great transition to my next question. I mentioned in my opening statement that in meetings I had last week with some building trades people in Connecticut, there were great complaints about the fact that they just

did not see much work, and it was particularly perplexing because I had convened a meeting either right before the Stimulus Act was adopted or right afterward with the State Transportation Department, construction firms, and labor unions, and the State said the jobs were permitted and ready to go when the money came forward.

My staff did some background on this, and unfortunately, it ended up with a result that was unsettling and dismaying to me about my own State, but I want to ask you if it is a broader problem. I am going to ask the State of Connecticut to respond as well, but here is what I found.

I am using the language of obligations, money authorized, and actual outlays, money actually spent. According to the numbers we found, the State of Connecticut received a total of \$454 million for highway and mass transit through the middle of last month. Approximately 59 percent, or \$269 million of the Stimulus Act funds have been obligated, in this case meaning that the project is officially chosen and the Department of Transportation has been notified. But here is the stunning number to me. Only \$506,000 of that has been outlaid in the State. Now, in checking, that turns out to be one of the lowest payout rates in the country, according to the White House.

So I wanted to ask you, from your perspective overseeing this program, what is happening there? Is this occurring in a lot of other States? And if so, what is the Administration doing about it, or what can the Administration do about it?

Mr. NABORS. It is something that we are seeing in a variety of different States. I think Connecticut is on the extreme side of things. I think there are two issues here. One is that, as I had mentioned previously, this is a relatively unique aspect of the Highway Transportation Fund and other transportation monies, and I think that in part, what has occurred is the State transportation offices have gotten used to doing business the same way every year with regard to their normal money. If you were looking at their annual appropriations, this would be a similar type of pattern that you would see.

What we are doing and what the Vice President is personally doing is reaching out directly to the governors and the State legislatures and saying, this isn't a normal time. We need to make sure that the money is getting out the door and stimulating the economy in a much more direct way. And people are being responsive to those requests and we will continue to make those requests of the States.

Chairman LIEBERMAN. Thank you. Thanks, Senator Collins.

Senator COLLINS. Thank you, Mr. Chairman.

Mr. Mihm, let me follow up on the issue of how we track the number of jobs that have been either created or saved by the Recovery Act. For most of us, looking at the job creation or the job saved numbers is a very important measure of whether the stimulus bill is achieving the goals that those of us who supported it hoped for. OMB is allowing two different methods for counting the jobs created or saved under the bill. The first is direct counting. It is obvious what that means. But OMB also allows a second option,

which is an extrapolation, an estimate based on project information.

My concern about having two different methods of measuring job creation or the number of jobs saved is that it could serve to undermine the public's confidence in the credibility of the numbers. Could you comment on the issue of whether we need two different ways, or whether we just need one set or one approach to measuring jobs created or saved?

Mr. MIHM. That is exactly one of the questions we are going to be looking at as we look at these recipient reports, is the methodologies they used. First, is there transparency in the reporting as to which methodology did they use? That is, does a user of this understand how they got the number? And then, second, as we do our assessments, does it make sense at a high level why people would choose one methodology over another? That is, is it done for all the right reasons?

Our approach is, over the next couple of weeks, our State teams that are out there in those 16 States and the District are sitting down with officials in the States, or the direct recipients who will be doing the reporting to Federalreporting.gov, and understanding what are the controls that you are going to have in place. How are you going to be reporting on the jobs? To the extent that you are relying on information from sub-recipients, what are you going to be doing to assure yourselves that you get good data? That is all before the reporting takes place.

And then after the reports come in, we are going to go back out there and say, did you actually do what you said you were going to do? And then beyond that, then test for some sub-recipients. Go down and find out that it flows all the way down.

As I mentioned earlier, our primary focus is going to be this time around on transportation programs, highway programs, because that is where a lot of the money is already and that is also, and my economist friends tell me that is where we can expect job impacts to the extent that we are going to see them.

So that is going to be the focus, but you are asking exactly the right question. The transparency on that is going to be very important.

Senator COLLINS. It is critical. I am very pleased that Maine has the opposite situation of Connecticut. We rank first in the Nation in the expenditure of stimulus funds for transportation projects. And it was very heartening to me to meet recently with the owner of a construction company who told me that there were 100 people working who otherwise would not have been, just on this one particular project.

But it also became clear to me that this becomes very complicated on how you count. If you have a project with 100 people working on it, that project ends and then there is another project that hires 50 of those people, how is that measured? Are those 50 new jobs, so the total is 150? Or is that a subset of the 100 that was originally counted? It becomes difficult, and the problems are obvious as you try to measure this, which is why I think it is important that we have an agreed-upon measurement system and just stick with it so the same standards are used everywhere and we have apples to apples.

Mr. MIHM. On the particular example that you are talking about——

Senator COLLINS. Yes.

Mr. MIHM [continuing]. And I will obviously defer to Mr. Nabors on this, but OMB has tried to address that by asking recipients to report on a full-time equivalent basis rather than on a specific job so that we do not get into these——

Senator COLLINS. Double-counting——

Mr. MIHM [continuing]. Types of situations, because the one you were describing, an argument could be made, well, did that second job then kill 50 jobs, and that is not what we are trying to get at.

Senator COLLINS. Right.

Mr. MIHM. And so the full-time equivalent calculation is designed to make sure we are comparing apples and apples across the board.

Senator COLLINS. Thank you.

Mr. Leibowitz, I want to go back to the issue that Senator McCaskill raised about what happens to these con artists. The FTC does a terrific job of shutting down the Web sites, doing the sweeps, but obviously you cannot cuff them, as she puts it, or you cannot prosecute it. You have to refer the case to the Justice Department.

Mr. LEIBOWITZ. Sure.

Senator COLLINS. So that raises the question, is the Justice Department receptive to pursuing these cases? What you always wonder and you always worry about, and I have done a lot of work over the decades on consumer fraud issues, the fear is that it is viewed as small potatoes and thus a case is never brought unless it reaches a certain threshold. And what happens, particularly in the Internet age, is that a con artist then goes on to set up another Web site and scams the next set of victims. That is closed down. The prosecution is declined because it is small again, although it is probably not because the range of victims is probably far greater than is realized. But how receptive is the Justice Department to following through on these cases?

Mr. LEIBOWITZ. Well, you have identified all of the problems and you did it without a diatribe, by the way. [Laughter.]

We work with the Justice Department. There is always a tension, and I have been on the Commission for 5 years, so there is always a tension at the Justice Department between the things that are their highest priorities—terrorism, hard-core crime—and things like fraud, which sometimes fall through the cracks.

But Attorney General Eric Holder and Lanny Breuer, who is the head of the Criminal Division, have both been very receptive to the idea of bringing more cases. We also have relationships with Assistant U.S. Attorneys and U.S. Attorneys, so we go directly to where the malefactors are. And, in fact, my recollection is, and I will check this and get back to you, that in one of the cases that we brought, Grant Connect, one of the malefactors is actually in jail now, or the husband who started the scam that was taken over by his wife who is actually the former Mrs. Nevada, is in jail.

So we are pretty good at getting cases to the Justice Department and the folks who can put these bad guys in jail. We have a Criminal Liaison Unit that has been great at referring cases. But it is an ongoing effort. On the other hand, we also respect the Justice

Department's priorities and so we want to be in there as quickly as we can.

But I will get back to you on that particular case and we will keep the effort up. And again, they have been very receptive at the Justice Department.

Senator COLLINS. Thank you.

Mr. Devaney, I am not familiar with the story that Senator McCaskill brought up this morning. While there are obvious issues with Congressional oversight, accountability, and transparency with the creation of new czar positions within the Executive Office of the President, that is a totally different issue from Senate-confirmed individuals who are performing important roles who do testify before us regularly. Although I am not familiar with the report that Senator McCaskill brought up, it is extremely unfair if your position is being lumped into the category with these other issues.

Let me just ask you one quick final question. You brought up a difficult issue in passing, and that is you said that the board that you are overseeing is not involved in making judgments about the quality of projects for which stimulus money is spent and that you are focused, if there is a direct bar against funding an aquarium, for example, then you would come into play, or if there is fraud, obviously, or improper payments.

But that raises a question of whether there is a gap here, because there are some projects that have been reported in the press, for example, building a guard rail around an evaporated lake, that clearly should not be funded. And traditionally, I have looked to the GAO or the IG to identify those projects. So if it is not your job to raise a red flag on those projects, and I understand why you think it may not be, whose job is it?

Mr. DEVANEY. Well, we are seeing things like that, and when we do, we bring that to the attention of either the agency directly, and we have made a lot of referrals directly to the agencies, you need to look at this, and also OMB. And reflecting back on something Mr. Nabors said earlier, there is a very aggressive approach on the part of the Vice President and his staff to get right on this. I mean, if they see something like that, my observation is, from a distance, they have been very aggressive about that.

I suspect when the data starts to roll in, we will see more of that. We will see more questionable projects. And we certainly are going to make sure that all that information that we get in the data gets out to the right people, gets over to the Department so they can look at that project to see if it was approved, if it was not approved, and do some watchful thinking about whether or not that was a smart thing to do.

But there are going to be projects that two or three people look at in very different ways. Was that a smart bridge or was that a bridge to nowhere? There are going to be a lot of opinions out there when people see this data, and that is what I meant earlier about sort of it is going to be an interesting time when people get to see that. We do not want to get involved in those sort of subjective judgments and want to be very clear about that, but nonetheless, if we see something that we think is clearly wrong, we are going to make sure that gets sent to the right place.

Senator COLLINS. Thank you.

Mr. Chairman, I just want to thank you for your leadership on this set of hearings that we have been holding. As you mentioned, this is the fifth oversight hearing, and I also want to thank their staff for their work. I particularly want to thank the staff for their work on the consumer fraud issues. I have long been very interested in those issues, since my days in State government and also as Chairman of the Permanent Subcommittee on Investigations, and I appreciate your including that aspect in this hearing. Thank you.

Chairman LIEBERMAN. Thank you, Senator Collins. Thank you for your leadership in all the efforts that were leading up to this hearing, and I appreciate also the work that your staff did on the consumer protection part of the hearing and the work that both of our staffs did together on the overall hearing.

I must say, I am proud of the Members of the Committee. I thought the questions were thoughtful. There were one or two diatribes, but— [Laughter.]

This is exactly what we want to do here. My net impression is that the Stimulus Act is having a positive effect on the economy. It is not perfect. I appreciate the fact, Mr. Nabors, that you said the Administration, with the Vice President leading the effort, is particularly committed to trying to accelerate the spending, and the Vice President in his characteristic way is hands on. I thought it was very important that you told me that he is on the phone himself calling governors in States where the rate of spending, or outlay, actual spending, is not what we hoped it would be. And I thank you, Mr. Devaney and Mr. Mihm, for the work that you are doing to assist us in our oversight.

This was an extraordinary legislative act with an enormous amount of money in it. We did it because of the sense of urgency we had about where our economy was heading. We worried it was heading over the cliff. We are comforted to feel now that it is not anywhere near the cliff, but still there is a lot of suffering.

But the bottom line here is that with this much money being spent this quickly, we feel ourselves a sense of accountability and responsibility, and you are out there working for us in the various ways you are, sharing that responsibility, and it is comforting to us. The reward for all your good work is that we are probably going to call you back here sometime at the end of October or early November, particularly after the Recovery.gov gets up and we begin to receive some of those recipient reports to see what that tells us about how we are doing.

Mr. Leibowitz, you added a very important dimension here and I appreciate that you were here. You can tell from both the public questioning by the Members, and I can tell you from the sort of private conversations as people were coming by the chair here, that Members are very interested and concerned about the scam artists. It has been a long time since I have heard the term "pond scum." It strikes me that we are in an age where we may soon be referring to "iPod scums," not pond scum. [Laughter.]

In any case, there is real interest in the Committee in exploring whether there are any changes in law that can improve or strengthen the work that you are doing by way of deterrence, by putting more power in the hands of not only the Commission, but



the Justice Department. So I ask that you work with our staff and your staff work with ours to see if there is something constructive that we can do in that regard.

Mr. LEIBOWITZ. We would be delighted to do that. I have had discussions with Senator Collins, because she is the Ranking Member of our Appropriations Subcommittee. I will get back to you with a list, but part of it is growing the agency. We are 30 percent smaller than we were 30 years ago, even though the population has grown from 225 million to 305 million in the United States. Part of it is just having a stronger deterrent.

So one thing that we are interested in and that there is growing support for is giving us fining authority. Another is giving us easier rulemaking authority. In the Omnibus Appropriations Act, Congress gave us the ability to do a rulemaking involving mortgages under the Administrative Procedure Act rulemaking, which is easier rulemaking. We are under something more or less medieval called the Magnuson-Moss Act. And because of that, we will do something very useful that sets a clear baseline.

So thank you for that support, and we are going to stay on top of this issue and we will get back to you——

Chairman LIEBERMAN. Good. We will work together on it.

Thank you all. The record of the hearing will be held open for 15 days for any additional questions or statements Members would like to submit.

With that, I thank you very much for your very important public service.

The hearing is adjourned.

[Whereupon, at 12:22 p.m., the Committee was adjourned.]



# A P P E N D I X

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**Prepared Statement of Chairman Joseph Lieberman  
“Follow the Money: Transparency and Accountability for Recovery and Reinvestment  
Spending”  
March 5, 2009**

Good morning and welcome to today’s hearing: “Follow the Money: Transparency and Accountability for Recovery and Reinvestment Spending.” Our purpose today is to examine how the federal government will account for the hundreds of billions of dollars that will be spent over the next two years and beyond as part of the American Recovery and Reinvestment Act.

It is our Committee’s responsibility under our traditional governmental affairs role to study “the efficiency, economy, and effectiveness of all agencies and departments of the Government.”

We take that responsibility seriously and we intend to ensure that measures are put in place to prevent cost overruns, provide strict oversight of contractor performance, and ensure that grant conditions are met, and that fraud is promptly prosecuted in all aspects of stimulus spending – which is truly unprecedented in the amount of money Congress has appropriated and the speed with which we have asked our government to spend it.

I want to thank our witnesses – Rob Nabors the Deputy Director at the Office of Management and Budget, Gene Dodaro the Acting Comptroller General, and Phyllis K. Fong, Inspector General of the Department of Agriculture who chairs the Council of the Inspectors General on Integrity and Efficiency - for coming in today. Each of them has a critical role to play in ensuring that these stimulus funds are not just spent quickly to help our economy, but effectively to protect our taxpayers.

History can be our guide in this. Seventy six years ago yesterday, President Franklin Roosevelt began his famed “first 100 days” with his first inaugural address to a nation then mired in the Great Depression. Unemployment was around 25 percent.

In his address, Roosevelt told an anxious nation that – I quote: “Our greatest primary task is to put people to work. This is no unsolvable problem if we face it wisely and courageously. It can be accomplished in part by direct recruiting by the Government itself, treating the task as we would treat the emergency of a war, but at the same time, through this employment, accomplishing greatly needed projects to stimulate and reorganize the use of our natural resources.” End of quote. That fits quite perfectly the aim most Members of Congress who voted for the stimulus had in their minds.

Ultimately the New Deal put eight million Americans back to work laying 650,000 miles of roads that speeded commerce; constructing the Bonneville and Grand Coulee dams that brought electricity into rural homes; erecting airports, like La Guardia in New York City, which became the hubs of a modern transportation infrastructure, along with the construction of thousands of other public buildings and parks we still use today.

By the end of Roosevelt's first term, the unemployment rate had been cut in half. We hope to see a similar cut at the end of President Obama's term.

The American Recovery and Reinvestment Act is similarly ambitious, seeking to save or create four million jobs by putting Americans to work in traditional infrastructure projects, like roads, bridges and buildings, but also by laying the groundwork for a 21<sup>st</sup> Century economy with investments in clean renewable energy, high-speed rail, computerized health care records and expanded broadband access across the nation.

With these investments, we will not only create millions of jobs in the short term, but can emerge from the current recession with the tools, physical assets, and a workforce with the skills that will make our economy even more productive in the long term.

But the history of the New Deal also offers some cautions as we embark on this massive stimulus program. Not all the New Deal projects left the kinds of grand legacies as the ones I mentioned earlier.

In the nation's capital, 100 people were hired to scare pigeons. In New York, people were put to work as fire hydrant decorators. The federal government funded a study on the production and efficiency of safety pins.

So frequent were these dubious projects that the word "boondoggle" was born to describe any job or program that wasted money and produced trivial results.

In fact, so common was this criticism that Roosevelt felt obliged to defend it, saying: "If we can boondoggle ourselves out of this Depression, that word is going to be enshrined in the hearts of the American people for years to come."

That's not the way it has worked out. Today we all know and disdain boondoggles. And while we understand that our economy needs a jolt, we want to make sure that every dollar of the \$500 billion the Recovery Act targets for spending on projects and programs will be used to restart the economy with not a penny lost, wasted or stolen.

We understand that speed is important, but we must not repeat the kind of mistakes that occurred in support of Iraqi reconstruction projects or in the aftermath of Hurricane Katrina where money was rushed out the door with little accountability and billions were wasted. We think we're off to a good start with some specific provisions of the Recovery Act legislation that put us in a position to protect taxpayers through spending of this money.

First, the legislation includes about \$250 million in additional funding for inspectors general to hire experienced auditors and investigators. The IGs are already designing proactive measures to ensure the stimulus money is spent properly.

Second, the legislation also creates the Recovery Accountability and Transparency Board, which will be headed by Earl Devaney, the Inspector General of the Interior Department,

who was appointed to the post last week by the President – and at least 10 inspectors general from departments and agencies that have some jurisdiction over the recovery package. This board is meant to ensure coordinated and comprehensive oversight of stimulus spending and provide regular reports to Congress and the public.

Mr. Devaney is just getting up and running, and I look forward to having him testify before the Committee at a future hearing.

Third, the Recovery Act adds protection for whistleblowers who work for state or local governments or for private contractors, who generally have no federal protection against retaliation if they disclose waste or fraud in the spending of federal stimulus funds. Some of the most significant information we get comes from people in the middle of the system, and they deserve whistleblower protection.

Fourth, a special website called Recovery.gov will provide transparency by posting information about spending, including grants, contracts, and all oversight activities, so that any American will be able to report on waste, fraud or abuse when they see it.

We want to work closely with the Obama Administration to make sure we have the manpower and systems in place to do the job right and safeguard the taxpayers' investments. The last think we need is waste and fraud in the spending of the billions of dollars of stimulus funds, which would break the public's confidence in their government just when we need it the most.

That is why our Committee is giving notice with this hearing today that we will monitor spending of stimulus money and oversee those who have the responsibility oversee stimulus spending.

Prepared Statement of  
Senator Susan M. Collins

'Follow the Money: Transparency and Accountability for Recovery and  
Reinvestment Spending'

March 5, 2009

Over the past year and a half, we have witnessed the collapse of the housing market, the unraveling of our nation's financial institutions, and the evaporation of trillions of dollars in the stock market and in people's retirement accounts.

The financial crisis that started on Wall Street has become a crisis on Main Street in every community in America. Nearly 600,000 Americans lost their jobs in the month of January alone, bringing the total number lost since the end of the summer to 2.5 million. The nation's unemployment rate is the highest it has been in more than 16 years.

That is why the stimulus bill we passed a few weeks ago is so critical. The economic stimulus package contains robust infrastructure spending, significant funding for state aid, tax relief for low- and middle-income families, and incentives for small businesses. It will save or create an estimated 3.5 million jobs. The investments in that bill should help turn this economy around. To be successful, however, these stimulus funds must be spent effectively and with transparency and accountability. They cannot be lost to waste, fraud, and mismanagement.

If these funds are not awarded in a timely, transparent, and appropriate manner, the impact of the economic stimulus package on the recovery will be blunted, and the results – whether for new jobs, better roads and schools, or other critical investments – will fall short of our expectations.

When there is a lack of accountability of federal funds aimed at stabilizing the economy, goals are not accomplished, and public support evaporates.

To avoid the oversight flaws of the TARP and help prevent similar abuse of stimulus funds, Congress included strong safeguards in the economic stimulus bill. These protections will help ensure aggressive oversight, enhanced transparency, and accountability for taxpayer dollars. The law includes additional funding for agency Inspectors General and the Government Accountability Office – government watchdogs charged with specific stimulus oversight.

The law also creates the "Recovery Act Transparency Board" to coordinate federal oversight efforts. A new website, Recovery.gov, will allow the public to access information on how stimulus money is being spent. The more eyes looking at this spending, the better.

Ensuring stimulus funds are spent properly also requires an effective acquisition workforce to develop and monitor stimulus contracts. Federal contract purchases now exceed \$532 billion a year, yet the federal government has entered the 21st Century with 22 percent

fewer federal civilian acquisition personnel than it had at the start of the 1990s. This means that as our contract spending continues to increase dramatically, our contracting workforce continues to shrink. Now the down-sized and shrinking acquisition workforce must effectively manage their existing responsibilities in addition to new stimulus contracts.

And acquisition workforce challenges may be more pronounced in states and local communities. As Allan Burman, former head of the Office of Federal Procurement Policy, has pointed out, the lack of adequate numbers of well-trained acquisition personnel at the federal, state, and local level could inhibit the up-front planning necessary for effective contracting. Whether in Iraq reconstruction, Hurricane Katrina-related contracts, or in numerous other contexts, a lack of planning has produced egregious examples of waste.

Today's hearing will examine the Administration's plans to safeguard the taxpayers' interests in the economic stimulus plan.

Our government has an obligation to make sure these funds are spent wisely so that they will have the maximum positive impact on our economy. America's families, struggling with the economic downturn, deserve no less.

**PREPARED STATEMENT OF  
SENATOR GEORGE V. VOINOVICH**

**FOLLOW THE MONEY: TRANSPARENCY AND ACCOUNTABILITY FOR RECOVERY AND  
REINVESTMENT SPENDING**

**THURSDAY, MARCH 5, 2009**

Mr Chairman, I want to thank you for holding this hearing. The American Recovery and Reinvestment Act of 2009 provides almost \$790 billion and we must do everything in our power to ensure that money is spent wisely, especially considering that the bill will add more than \$1.1 trillion to the national debt over 10 years.

I am concerned, not only by the sheer amount of money being spent under this bill, but also by the speed with which the money will be spent.

I understand the Administration and Congress are anxious to get money on the street for shovel ready projects, but I am concerned that we do not have the human capital necessary to achieve the results intended by this law while also conducting regular government operations. As the Professional Services Council has noted, "[w]ithout a government workforce sufficient to plan, deliver and manage the contracts and grants that dispense these huge funds, it will be like constructing an office building on a foundation of sand."

Further, while I support the bill's provisions that provide our inspectors general with more resources to review stimulus expenditures after the fact, I do not think that alone will prevent the waste, fraud and abuse this spending will be prone to.

I also question whether our current compliment of inspectors general have the capacity to conduct the oversight and investigations that are required by this law and also carry out their already assigned responsibilities under the Inspector General Act.

I look forward to hearing from our witnesses today about plans to ensure that these historical expenditures are spent wisely and appropriately.

Thank you, Mr. Chairman.



**Testimony of Robert Nabors**  
**Deputy Director, Office of Management and Budget**  
**Senate Homeland Security and Governmental Affairs Committee**  
**March 5, 2009**

Chairman Lieberman, Ranking Member Collins, distinguished Members of the Committee, thank you for inviting me to testify before you today about the implementation of the American Recovery and Reinvestment Act, signed into law just a few short weeks ago.

As you know, the Recovery Act was an urgent and necessary response to the dire crisis that our economy faces.

We are in a deep recession, which threatens to be more severe than any since the Great Depression. More than three and a half million jobs were lost over the past 13 months, more than at any time since World War II. And GDP declined at an annual rate of 6.2 percent in the fourth quarter of the last year – the highest rate in over 25 years.

Every community and sector of our economy has been affected by this recession. Manufacturing employment has hit a 60-year low. Capital markets are virtually frozen, making it difficult for businesses to grow and for families to borrow money to afford a home, car, or college education for their kids. Trillions of dollars of wealth have been wiped out, leaving many workers with little or nothing as they approach retirement.

In essence, we face a widening gap between what our economy is capable of producing and what it is actually producing. Equal to about \$1 trillion in 2009, this output gap is equivalent to roughly 7 percent of the estimated potential output of our economy. Restoring the demand for goods and services that our economy could produce with its existing capacity is the key to returning the nation to a path of economic growth.

That's why the President signed the Recovery Act, which is intended to provide relief to millions of struggling families, jumpstart our economy, create or save more than 3.5 million jobs over the next two years, and steer our nation out of this recession and towards a path of long-term prosperity. The investments the Act makes now in infrastructure, health care, education, and clean energy will create jobs and also lay a foundation upon which the American economy can grow in the future.

Passing this Act was an important step towards immediate recovery and the restoration of long-term fiscal stability. But for the Recovery Act to be effective, funds need to be spent quickly and wisely. Allow me to say a few words about the work we are doing to accomplish both of these objectives.

**First, for the Recovery Act to have the desired effect, funds must reach recipients quickly.**

Since the Act was signed, the Administration has been working quickly to channel funding into our struggling economy. Already, more than \$15 billion of Medicaid grant awards have been allocated, covering the first two quarters of fiscal year 2009. In addition, \$10 billion has been allocated to create green jobs, revive housing markets with high rates of foreclosure, and curb homelessness. New funds for unemployment insurance and food stamps; grants to hire more police officers and for workforce development; block grants to States and localities; dam and levee funding; and formula funding for highway and other transit construction has been allocated or will be this month.

We are doing our part to expedite this process by working to make our application processes and guidance as clear as possible so that funds reach the hands of those who need them, as quickly as possible. But we need the help of our State and local partners to ensure that Recovery funding makes its way into the economy. States can't let Recovery Act funds sit in "rainy day" accounts. And Recovery Act funding shouldn't be used to reimburse programs for previous expenses.

**Second, it is essential that funds be spent wisely at all levels of government, and in a way that maintains the confidence of the public.**

The President understands the magnitude of government's responsibility in managing taxpayer dollars. This is precisely why the Recovery Act was designed to ensure unprecedented levels of transparency and accountability, and why the Administration has moved swiftly to implement both the leadership and the internal processes necessary to oversee this massive effort.

In terms of leadership, the President designated Vice President Biden as the Administration's point person to coordinate the Federal response on the Recovery Act. He also named Earl Devaney – the Inspector General of the Department of the Interior and a public servant with a record of uncovering waste, fraud, and abuse – as the head of the Recovery oversight board.

On process, the day the Recovery Act was signed, the Administration launched Recovery.gov, a website that will empower citizens to hold the government accountable by reporting where Recovery dollars are going and how they are being spent. The response has been significant. Recovery.gov received 3,000 hits per second the moment it was launched, and has received over 150 million hits since February 17. As funds make their way to projects, we anticipate that the website will be a valuable resource for tracking their use.

In this very early phase of Recovery Act implementation, we are focusing on ensuring that the federal agencies tasked with managing Recovery money are executing their mandates well. OMB has transmitted detailed guidance to all of the agencies on how to manage Recovery Act dollars in a way that will promote transparency and efficiency.

The guidance calls on agencies to go beyond standard operating procedures and recognize the unusual nature of Recovery funds. Agencies are required to ensure that Recovery money is distinguished from other funding in their financial systems, grant and contract writing systems, and reporting systems. For example, within their financial systems, agencies are generally required to set up unique treasury appropriation fund symbols for all Recovery Act funding.

We have emphasized the extraordinary responsibility that falls on all government workers to prove to the American people that we are spending their dollars well. To inform citizens how, when, and where Recovery dollars are being spent, the guidance presents new, tight reporting deadlines. This week, agencies began submitting weekly reports that provide a breakdown of funding, noteworthy actions to-date, and major planned actions. By no later than May 1, we have asked that they submit both an "Agency Recovery Plan" and separate "Recovery Program Plans" for each program named in the Act.

The agencies' spending plans will be comprehensive, publicly available, and will detail all critical areas of program implementation, including:

- Funding amounts and timeframes;
- Methods of awarding dollars;
- Specific activities to be funded;
- Key milestones and deadlines;
- Steps taken to comply with relevant environmental requirements;
- Program objectives and goals;
- Measurements of performance and integrity; and
- Measures to ensure accountability for results.

We have also asked for monthly financial reports and detailed data submissions on award transactions – beginning in early May.

Within OMB, we closely monitor milestones, obstacles, and other significant issues pertaining to the implementation of agency Recovery plans, as well as the use of specific funds. We work to ensure that matters of significance are appropriately brought to the attention of senior Administration officials on a daily basis so that they can be resolved.

However, the Administration cannot achieve the goals of unprecedented transparency and accountability without help from Congress and State and local governments. All levels of government share responsibly for rooting out error and waste, and ensuring that only the most worthy projects receive precious Recovery dollars. These projects should meet high standards of economic value and equally high standards when judged by the public for fairness and impartiality.

No one should doubt the importance of the Recovery Act in creating jobs, restoring public confidence in our economy, and putting our nation back on track. Nor should anyone doubt the importance of implementing this Act as efficiently, transparently, and

effectively as possible. The American people have put their faith and confidence in us – their government – to take on a challenge too big for any other entity to tackle.

We are the ones entrusted with their hard-earned money. I look forward to working with the Members of this Committee in the months ahead to live up to their expectations, and deliver the transparency, accountability, and performance that we promised.

Thank you and I look forward to taking your questions.

United States Government Accountability Office

GAO

Testimony  
Before the Committee on Homeland  
Security and Governmental Affairs,  
U.S. Senate

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## AMERICAN RECOVERY AND REINVESTMENT ACT

### GAO's Role in Helping to Ensure Accountability and Transparency

Statement of Gene L. Dodaro  
Acting Comptroller General of the United States



GAO-09-453T

**GAO**  
Accountability Integrity Reliability  
**Highlights**

Highlights of GAO-09-453T, a report to the Committee on Homeland Security and Governmental Affairs, U.S. Senate

### Why GAO Did This Study

This testimony discusses GAO's plans to carry out its oversight role related to the American Recovery and Reinvestment Act of 2009 (Recovery Act). The Recovery Act funds are provided for purposes including: preserving and creating jobs and promoting economic recovery; assisting those most impacted by the recession; investing in transportation, environmental protection, and other infrastructure to provide long-term economic benefits; and stabilizing state and local government budgets.

The Recovery Act assigns GAO a range of responsibilities to help promote accountability and transparency. Some are recurring requirements such as providing bimonthly reviews of the use of funds by selected states and localities. Others include targeted studies in several areas such as small business lending, education, and trade adjustment assistance.

This statement discusses (1) GAO's plans to carry out its responsibilities under the Recovery Act, (2) how GAO's responsibilities relate to other oversight authorities, such as the Inspectors General (IG) and the Recovery Accountability and Transparency Board (Board), and (3) the challenges posed in ensuring accountability over the use of funds and associated lessons learned and best practices that can be helpful in addressing those challenges.

To view the full product, including the scope and methodology, click on GAO-09-453T. For more information, contact Stanley J. Czerwinski, (202) 512-6806, [czerwinski@gao.gov](mailto:czerwinski@gao.gov).

## AMERICAN RECOVERY AND REINVESTMENT ACT

### GAO's Role in Helping to Ensure Accountability and Transparency

#### What GAO Found

The Recovery Act delineates an important set of responsibilities for GAO and others in the accountability community. GAO's bimonthly reviews of selected states' and localities' uses of the Recovery Act funds will examine how funds are being used and achieving the stated purposes of the Recovery Act. GAO has selected a core group of 16 states to follow over the next few years to provide an ongoing longitudinal analysis of the use of funds under the Recovery Act. These states contain about 65 percent of the U.S. population and are estimated to receive about two-thirds of the intergovernmental grants funds available through the Recovery Act. In addition, GAO will sample localities within these states to provide a perspective on the use of funds at the local level. In addition to reporting on the core group of 16 states, GAO will be reviewing the recipient reports from all 50 states as part of its responsibilities to review these filings. Depending on those assessments and other risk-based analyses, GAO's reviews may include additional states, localities, or other recipients as implementation proceeds.

GAO is charged with reviewing the use of funds by selected states and localities. IGs across government are expected to audit the efforts of federal agencies' operations and programs related to the Recovery Act, both individually within their particular entities and collectively, as many of them are members of the Board. Because funding streams for the Recovery Act will flow to states and localities from different federal agencies, it is important for GAO to coordinate with the IGs and the Board, which is charged with coordinating and conducting oversight of Recovery Act funds in order to prevent fraud, waste, and abuse. Among other things, the Board is to review contracts and grants to ensure they meet applicable standards. It is also important for GAO to coordinate with the Office of Management and Budget, especially with regard to reporting requirements and other guidance to fund recipients and on what information should be collected in order to adequately evaluate how well the Recovery Act achieves its objectives.

There are many implementation challenges to ensuring adequate accountability and efficient and effective implementation of the Recovery Act. Experience tells us that the risk for fraud and abuse grows when billions of dollars are going out quickly, eligibility requirements are being established or changed, and new programs are being created. This suggests the need for a risk-based approach for targeting attention on specific programs and funding structures early on based on known strengths, vulnerabilities, and weaknesses such as a track record of improper payments or contracting problems. In that regard, the accountability community has, in recent years, produced a wide variety of best practices and related guides, which are available to agencies to assist them in ensuring they have the needed internal controls in place from the outset. These best practices and related guides cover such areas as fraud prevention, contract management, and grants accountability.

United States Government Accountability Office

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Chairman Lieberman, Ranking Member Collins, and Members of the Committee:

I am pleased to be here today to discuss how GAO plans to carry out its oversight role related to the American Recovery and Reinvestment Act of 2009 (Recovery Act).<sup>1</sup> Congress and the administration have fashioned a significant response to what is generally reported to be the Nation's most serious economic crisis since the Great Depression. The Congressional Budget Office (CBO) estimates that the Recovery Act's combined spending and tax provisions will cost \$787 billion, of which over \$580 billion will be in additional spending.

The Recovery Act assigns GAO a range of responsibilities to help promote accountability and transparency.<sup>2</sup> Some are recurring requirements such as, most prominently, conducting bimonthly reviews of the use by selected states and localities of funds made available under the act and commenting on the estimates of the number of jobs created and the number of jobs retained in the quarterly reports filed by recipients of funds under the Recovery Act. Others relate to specific areas including trade adjustment assistance, new education incentive grants, and efforts by the head of the Small Business Administration (SBA) to, among other things, increase the liquidity in the secondary market for small business loans. Still others include performing longer-term studies of the new health care tax credits and of the effects of national economic downturns on states over the past several decades—especially in the Medicaid area—leading to recommendations to help address those effects in the future.

As I will outline today, we have already begun the work of meeting these responsibilities and have reached out to the broader accountability community to start coordinating our respective roles, planned approaches, and timelines. This includes the Inspectors General (IG), state auditors, and local government auditors as well as the Chair of the Recovery Accountability and Transparency Board (Board). Collectively, the accountability community will play important roles in helping to ensure that Recovery Act funds are spent properly and meeting their intended purposes, as well as in identifying management or funding issues that need attention.

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<sup>1</sup>Pub. L. No. 111-5 (February 17, 2009).

<sup>2</sup>Appendix I to this statement lists the responsibilities assigned to GAO in the Recovery Act.

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My statement today discusses (1) GAO's plans to carry out its responsibilities under the Recovery Act, (2) how GAO's responsibilities relate to other oversight authorities, such as the IGs and the Board, and (3) the challenges posed in ensuring accountability and transparency of funds and the associated lessons learned and best practices that can be helpful in addressing those challenges.

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### GAO's Plans to Carry Out Its Recovery Act Responsibilities

Our bimonthly reviews of selected states' and localities' will examine how Recovery Act funds are being used and whether they are achieving the stated purposes of the act. These purposes include:

- to preserve and create jobs and promote economic recovery;
- to assist those most impacted by the recession;
- to invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits; and
- to stabilize state and local government budgets in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

We have selected a core group of 16 states that we will follow over the next few years to provide an ongoing longitudinal analysis of the use of funds under the Recovery Act. The states are Arizona, California, Colorado, Florida, Georgia, Iowa, Illinois, Massachusetts, Michigan, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas. These states contain about 65 percent of the U.S. population and are estimated to receive about two-thirds of the intergovernmental grants funds available through the Recovery Act. We selected these states on the basis of outlay projections, percentage of the U.S. population represented, unemployment rates and changes, and a mix of states' poverty levels, geographic coverage and representation of both urban and rural areas. In addition, we will sample localities within these states to provide a perspective on the use of Recovery Act funds at a local level.<sup>3</sup>

GAO will be reaching out to the respective governors' and state auditors' offices to begin the work needed for our first bimonthly review to be completed this April. In addition to reporting on the core group of 16

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<sup>3</sup>We will also include Washington D.C. in our selection of localities.



states, we will be reviewing the recipient reports from all 50 states as part of our responsibilities to review these filings. These recipient reports are to include information on funds received, the amount of recovery funds obligated or expended to projects or activities, and the projects or activities for which funds were obligated or expended. Depending on our assessments, we may visit states other than the 16 core group to review targeted areas. Finally, our Forensic Audits and Special Investigations unit (FSI) will be undertaking ongoing risk assessments to identify specific programs and funding streams that are especially vulnerable to fraud, and it will conduct targeted investigations based on its assessments.

In addition to our bimonthly reviews of selected states and localities, we also have efforts underway to meet two other short-term requirements. Specifically, within 45 days after the Recovery Act was signed—by April 3, 2009—we must make 13 appointments to the Health Information Technology (HIT) Policy Committee, which is to recommend a policy framework for development and adoption of a nationwide health information infrastructure to permit the electronic exchange and use of health information. On February 25, 2009, we placed a notice in the Federal Register to solicit nominations to the HIT Policy Committee. Also, within 60 days, we must report on the Small Business Administration's efforts to, among other things, increase liquidity in the secondary market for SBA loans, and our work on this review is well underway.

### How GAO's Responsibilities Relate to Other Oversight Authorities

The Recovery Act delineates an important set of responsibilities for the accountability community. GAO is charged with reviewing the use of funds by selected states and localities. IGs across government are expected to audit the efforts of federal agencies' operations and programs related to the Recovery Act, both individually within their particular entities and collectively, as many of them are members of the Board. The Recovery Act established the Board to help prevent waste, fraud, and abuse. The Board is to review contracts and grants to ensure they meet applicable standards, follow competition requirements, and are overseen by sufficient numbers of trained acquisition and grants personnel. The Board has a range of authorities and is charged with reporting to the President and Congress any potential problems requiring immediate attention in addition to reporting quarterly and annually.

Because funding streams of the Recovery Act will flow to the states and localities from different federal agencies, it is important for us to coordinate with the IGs and the Board. Consequently, soon after the act was passed, I reached out to the IG community and, with Ms. Phyllis Fong,

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the Chair of the Council of Inspectors General on Integrity and Efficiency (CIGIE), hosted an initial coordination meeting on February 25, 2009, with Inspectors General or their representatives from 17 agencies. It was a very productive discussion in which we outlined coordination approaches going forward.

Soon after the President appointed him as Chair of the Board on February 23, 2009, I talked with Mr. Earl Devaney, former Inspector General at the Department of the Interior. I am confident that we will coordinate our respective efforts well, both with the IG community and the Board. We work well together on other large coordination efforts such as the audit of the U.S. government's consolidated financial statements whereby GAO relies on the individual efforts of the IG's financial audits of their departments and entities across government.

We also have already reached out to the state and local audit community to have initial discussions and establish coordination approaches. On February 26, 2009, we participated in a conference call arranged by the National Association of State Auditors, Comptrollers and Treasurers with state auditors or their representatives from 46 states and the District of Columbia. On February 27, 2009, we held a similar discussion with local auditors from many localities throughout the country. State and local auditors perform very important oversight functions in their jurisdictions and have unique knowledge about their governments; we plan to coordinate with them closely in carrying out our responsibilities.

It is also important for us to coordinate with the Office of Management and Budget (OMB), especially in regard to reporting requirements and other guidance to fund recipients and on what information is to be collected in order to adequately evaluate how well the Recovery Act achieves its objectives. For example, OMB Director Peter Orszag and I have received a letter from the National Association of State Auditors, Comptrollers and Treasurers; the National Association of State Budget Officers; the National Association of State Chief Information Officers; and the National Association of State Procurement Officials. This letter expresses their strong interest in coordinating reporting and compliance aspects of the Recovery Act. I have been in contact with OMB and these groups, and we and OMB are undertaking discussions with them.

While there are many reporting and other implementation issues that lie ahead, we are encouraged by OMB's initial implementation guidance. In its guidance, OMB points out the need to balance the desire to get funds out

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quickly to help turn the economy around with the equally important need to make sure funds are spent properly, efficiently, and effectively.

One particular area that also needs attention is identifying the data to be collected concerning the use and results of the Recovery Act's various tax provisions. Accountability and transparency are perhaps easier to envision for the outlay portions of the stimulus package, but the billions of dollars in tax provisions in the Recovery Act are considerably different than outlay programs in their implementation, privacy protections, and oversight. Most tax benefits are entirely administered by the Internal Revenue Service (IRS), and all taxpayer information, including the identity of those using the benefits, is protected by law from disclosure. Further, unlike for most outlay programs, IRS does not know who makes use of the tax benefit until after the fact, if then.

In general, IRS does not collect information on who claims tax benefits and to what extent, unless it determines such information is necessary for tax administration. In part because of the Paperwork Reduction Act, IRS generally avoids collecting information not directly needed for tax administration because both taxpayers and IRS incur costs and other burdens associated with any information-reporting requirements. As a result, in the past, information often has not been available to help Congress determine the effectiveness of some tax provisions or even identify the numbers of taxpayers using some provisions.

For example, information was not available to Congress to determine the effect of the Empowerment Zone and Enterprise Community program on poverty, unemployment, and economic growth.<sup>4</sup> IRS did not collect information on who used some of the tax benefits or the communities where benefits were used, or both. The lack of data on the use of the Empowerment Zone and Enterprise Community tax benefits was of particular concern because the estimated amount of the tax benefits was greater than the amount of grant funds dedicated to the program. For instance, in the first round of the program, recipients received about \$1 billion in grants; the Joint Committee on Taxation had estimated that tax benefits would reduce federal revenues by \$2.5 billion between 1994 and 1998.

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<sup>4</sup>GAO, *Empowerment Zone and Enterprise Community Program: Improvements Occurred in Communities, but the Effect of the Program Is Unclear*, GAO-06-727 (Washington, D.C.: Sept. 22, 2006).

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Absent direction from the Department of the Treasury (Treasury) or OMB, IRS is unlikely to collect sufficient information to support congressional oversight of the act's tax provisions because some provisions have characteristics similar to existing provisions in other laws where we found insufficient information was collected to enable congressional oversight. Accordingly, we have reached out to both OMB and Treasury about their plans to collect and report data on the Recovery Act tax provisions. Both OMB and Treasury indicated they initially focused on the spending programs and not the tax provisions in the Recovery Act. They acknowledged that additional data beyond what IRS would normally collect may be needed and that they would consider the tax-data needs as they proceed.

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### Lessons Learned and Best Practices That Can Be Helpful in Addressing Challenges to Implementing the Recovery Act

There are many implementation challenges to ensuring adequate accountability and efficient and effective implementation of the Recovery Act. Experience tells us that the risk for fraud and abuse grows when billions of dollars are going out quickly, eligibility requirements are being established or changed, new programs are being created, or a mix of these characteristics. This suggests the need for a risk-based approach to target for attention specific programs and funding structures based on known strengths, vulnerabilities, and weaknesses, such as a track record of improper payments or contracting problems. In that regard, the accountability community has, in recent years, produced a wide variety of best practice and related guides, which are available to agencies to assist them in ensuring they have the needed internal controls in place from the outset. These best practice and related guides cover such areas as:

**Fraud Prevention:** By establishing an effective fraud prevention program, agencies can provide reasonable assurance that Recovery Act funds benefit intended recipients. A well-designed fraud prevention program—which can also minimize waste and abuse—should consist of preventive controls, detection and monitoring, and investigations and prosecutions. Our work has shown that building internal controls in up front is of the utmost importance and that fraud prevention is the most efficient and effective means to minimize fraud, waste, and abuse. Once federal dollars are disbursed fraudulently or improperly, the government is only likely to recover a few pennies on the dollar. Thus, preventive controls are the most important component of a fraud prevention system. These controls prevent ineligible individuals and questionable firms from gaining access to government funds in the first place.

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Our work across the government shows that agencies sometimes do not focus on the importance of preventive controls. Examples of preventive controls, based in part on our body of work that was focused on disaster relief after Hurricanes Katrina and Rita<sup>5</sup> include the following:

- validating data used in decision making against other government or third-party sources;
- inspecting whenever possible to confirm information prior to payment;
- conducting system edit checks to identify problems before payments are made; and
- training staff on fraud awareness.

In addition, we testified last week that businesses and individuals that have been excluded for egregious offenses ranging from national security violations to tax fraud are improperly receiving federal contracts and other funds.<sup>6</sup> Most recently, in February 2009, the National Procurement Fraud Task Force (NPFTF)<sup>7</sup> published a white paper<sup>8</sup> that identified best practices and made recommendations for agencies to consider in preventing fraud, waste, and abuse in grants they administer. These recommendations included enhanced certifications, increased training, improved communications with grant recipients, increased information sharing concerning potential fraud, and rigorous oversight of how grant dollars are spent after they are awarded.

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<sup>5</sup>GAO, *Individual Disaster Assistance Programs: Framework for Fraud Prevention, Detection, and Prosecution*, GAO-06-454T (Washington, D.C.: July 12, 2006); and GAO, *Hurricanes Katrina and Rita Disaster Relief: Prevention Is the Key to Minimizing Fraud, Waste and Abuse in Recovery Efforts*, GAO-07-418T (Washington, D.C.: Jan. 29, 2007).

<sup>6</sup>GAO, *Excluded Parties List System: Suspended and Debarred Businesses and Individuals Improperly Receive Federal Funds*, GAO-09-119T (Washington, D.C.: February 26, 2009).

<sup>7</sup>The NPFTF includes 58 prosecutorial and investigative agencies, including 35 Offices of Inspectors General. It is chaired by the Department of Justice's Assistant Attorney General of the Criminal Division and its goal is to detect, investigate, and prosecute procurement fraud, grant fraud, and associated corruption.

<sup>8</sup>National Procurement Fraud Task Force, Grant Fraud Committee, *A Guide to Grant Oversight and Best Practices for Combating Grant Fraud* (Washington, D.C.: February 2009).

**Contract Management:** Agencies that administer the Recovery Act funds will be expected to minimize fraud, waste, and abuse in contracting. Their procurement offices will need to be able to report data and statistics on the use of noncompetitive contract awards, contract types, the recipients of contracts, amounts of awards and the type of projects for which government funds are awarded. We have also learned from our body of work examining contracting after Hurricanes Katrina and Rita that best practices include developing knowledge of contracting capabilities before they are needed, establishing scalable operations plans that can adjust to the level of capacity required to effectively respond to the need, and providing sufficient numbers of field-level staff with the authority needed to meet mission requirements.<sup>9</sup> To prevent some of the problems that have affected previous federal contract spending such as for the Iraq war and recovery operations related to Hurricane Katrina, we have developed the following basic principles:

- Have transparent lines of procurement responsibility, authority, and oversight defined and in place.
- Ensure contracts are well structured by establishing clear requirements prior to award.
- Award contracts competitively.
- Use fixed-price contracts to the maximum extent possible.
- Ensure adherence to high ethical standards, including appropriately limiting state and local officials' employment by firms they supervised as government employees.
- Appoint contract surveillance personnel as early on as possible—preferably prior to or as soon as contracts are awarded—and ensure that these personnel have clear guidance and training as to their role and responsibilities and that there is clear responsibility for approving payments.
- Enforce penalties for companies and individuals that commit severe ethics violations or fail to demonstrate acceptable performance and refer suspected fraud to the appropriate agency promptly.
- Coordinate with state and local program officials and auditors in the planning and execution of contracts, agreements, and audits and other reviews.

In addition, we recently issued the GAO Cost Estimating and Assessment Guide as a helpful resource to agencies.<sup>10</sup> It will be especially helpful to agencies that will be administering large project contracts stemming from the use of Recovery Act funds. Congress, agencies, and the American

<sup>9</sup>GAO, *Hurricane Katrina: Improving Federal Contracting Practices in Disaster Recovery Operations*, GAO-06-714T (Washington, D.C.: May 4, 2006).

<sup>10</sup>GAO, *GAO Cost Estimating and Assessment Guide: Best Practices for Developing and Managing Capital Program Costs*, GAO-08-338P (Washington, D.C.: March 2008).

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public want to know whether government programs are achieving their goals and what their costs are. To make those evaluations, reliable cost information is required. We developed the Cost Guide in order to establish a consistent methodology that is based on best practices and that can be used across the federal government for developing, managing, and evaluating capital program cost estimates.

**Grants Accountability:** In 2005, the Domestic Working Group, made up of federal, state, and local audit organizations and chaired by the Comptroller General, developed a set of suggestions for improving grant accountability. In its report,<sup>11</sup> the Domestic Working Group highlighted what it called "promising practices" in the areas of internal control systems, performance measures, managing performance, the preaward process, and assessing and using results. Some specific examples of these practices included:

- assessing applicant capability to account for funds,
- including clear terms and conditions in grant award documents,
- providing grant-management training to staff and grantees,
- consolidating information systems to assist in managing grants,
- coordinating programs with similar goals and purposes,
- linking activities with program goals and working with grantees to develop performance measures, and
- monitoring the financial status of grants and monitoring subrecipients as a critical element of grant success.

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In summary, GAO welcomes the responsibility that Congress has placed on us to assist it in the oversight, accountability, and transparency of the Recovery Act. We will continue to coordinate closely with the rest of the accountability community. We also are committed to completing our Recovery Act work on the timetable envisioned by the act and will keep the Congress fully informed as our plans evolve.

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<sup>11</sup>Domestic Working Group, Grant Accountability Project, *Guide to Opportunities for Improving Grant Accountability* (Washington, D.C.: October 2005).

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Mr. Chairman, Senator Collins, and Members of the Committee this concludes my statement. I would be pleased to respond to any questions you may have.



## Appendix I: GAO Mandates in the American Recovery and Reinvestment Act of 2009

Review or reporting date	Title	Section of the Recovery Act	Summary
April 3, 2009	Health IT Policy Committee Appointments	Division A, title XII, § 13101	The Comptroller General is required to appoint 13 members of the Health Information Technology (HIT) Policy Committee. The HIT Policy Committee is to make policy recommendations to the National Coordinator of Health Information Technology relating to the implementation of a nationwide health information technology infrastructure, including implementation of a strategic plan.
Bimonthly starting in April 2009	State and Local Use of Funds	Division A, title IX, § 901	GAO is required to conduct bimonthly reviews and prepare reports on such reviews on the use by selected states and localities of funds made available in the Recovery Act. The Recovery Act does not specify the criteria by which the states and localities will be selected. The reports are to be available online.
April 20, 2009	SBA Report	Division A, title V, § 507	GAO is required to report on the actions of the Small Business Administration (SBA) in implementing the authorities established in certain provisions of the Recovery Act. The report is to include a summary of the activity of SBA under these provisions and an analysis of whether SBA is increasing liquidity in the secondary market for SBA loans.
Each calendar quarter starting on August 25, 2009	Comments on Recipient Reports	Division A, title XV, § 1512	GAO, along with the Congressional Budget Office, is to comment on estimates of the numbers of jobs created and retained by projects and activities as reported by recipients of federal funds appropriated by the Recovery Act.
February 18, 2010	Treatment Disclosures	Division A, title XIII, § 13424	GAO is required to report on the best practices related to the disclosure among health care providers of protected health information of individuals for purposes of treatment. The report is to include an examination of the best practices implemented by states and other entities; the extent to which these best practices improve the quality of the health care provided to individuals; the ability of health care providers to manage the best practices; and the use of electronic informed consent for disclosing protected health information for treatment, payment, and health care operations.

Review or reporting date	Title	Section of the Recovery Act	Summary
March 1, 2010	Health Tax Credit	Division B, title I, § 1899L	GAO is required to perform a study regarding the health care credit allowed under section 35 of the Internal Revenue Code, and report on the results of the study and include in the report an analysis of the administrative costs of the federal government and qualified health insurance providers; the health status and relative risk status of individuals covered under by qualified health insurance; the participation in the health care credit any advance payments under the credit; and the extent to which covered individuals obtained health insurance other than qualifying health insurance or went without health insurance.
Each year starting between March 15 and April 15, 2010, until the minimum wage in the respective territory is \$7.25 per hour	Minimum Wage	Division A, title VIII, § 802	GAO is required to study and report on the impact of 2007 and 2008 increases in the minimum wage in American Samoa and the Commonwealth of the Northern Mariana Islands on the rates of employment and the living standards of workers, and estimate the impact of any further wage increases on rates of employment and the living standards of workers in those territories, with full consideration of other factors that may impact the rates of employment and the living standards of workers, including how the profitability of major private sector firms may be impacted by wage increases in comparison to other factors such as energy costs and the value of tax benefits.
August 18, 2010	HIPPA Enforcement	Division A, title XIII, § 13410	GAO is required to submit a report including a recommendation of a methodology under which an individual who is harmed by certain offenses under HIPPA relating to privacy or security may receive a percentage of any civil monetary penalty or monetary settlement.
April 1, 2011	Economic Downturn	Division B, title V, § 5008	GAO is to study and report on periods of national economic downturn since 1974, including the current one, for the purpose of developing recommendations for addressing the needs of states during such periods. The study is to include an analysis of the past and projected effects of temporary increases in the federal medical assistance percentage under the Medicare program with respect to such periods. The report is to include, among other things, recommendations for modifying the national economic downturn assistance formula for temporary adjustment of the federal medical assistance percentage under Medicaid to improve the effectiveness of the application of such percentage in addressing the needs of states.
September 30, 2012	Trade Report	Division B, title I, § 1894	GAO is to comprehensively report on the operation and effectiveness of certain amendments made by the Recovery Act to the Trade Act of 1974.

Review or reporting date	Title	Section of the Recovery Act	Summary
February 18, 2014	Health Report	Division A, title XIII, § 13424	GAO is to report on the impact of the Recovery Act on health insurance premiums, overall health care costs, adoption of electronic health records by providers, and reduction in medical errors and other quality improvements.
No deadline specified in the Recovery Act	Education Grants	Division A, title XIV, § 14009	GAO is to evaluate certain programs related to education. The evaluation is to include the criteria used for the awards made, the states selected for awards, award amounts, how each state used the award received, and the impact of this funding on progress made toward closing achievement gaps.

UNITED STATES DEPARTMENT OF AGRICULTURE  
OFFICE OF INSPECTOR GENERAL

STATEMENT OF THE HONORABLE PHYLLIS K. FONG  
INSPECTOR GENERAL

Before the  
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE

MARCH 5, 2009



Good morning, Chairman Lieberman, Ranking Member Collins, and Members of the Committee. Thank you for inviting me to testify on the role of the Inspector General (IG) community in overseeing Federal expenditures and operations under the American Recovery and Reinvestment Act of 2009 (Recovery Act).<sup>1</sup> I am testifying today in my dual capacities as Inspector General at the U.S. Department of Agriculture (USDA) and Chair of the Council of the Inspectors General on Integrity and Efficiency (Council). Additionally, as IG at USDA, I am statutorily appointed to serve with nine other IGs on the Recovery Accountability and Transparency Board (Board) that was created by the Act. I am honored to serve in these multiple capacities and have the opportunity to contribute to our mutual efforts to improve the operations and integrity of the Federal Government.

Let me briefly also express my thanks to the Chair, Ranking Member Collins, and Senator McCaskill for soliciting the views of the IG community during the development and passage of the Act. My colleagues and I appreciate your affording us the opportunity to comment upon the practical impact of the provisions related to the Accountability Board and whistleblower complaints, among others. Further, your support for increased resources for IGs to meet our expanded responsibilities under the Recovery Act was of considerable assistance.

The Recovery Act creates a vital oversight role for the IG community, and I can assure the Committee that the IGs at the agencies that are receiving stimulus funds are actively engaged in planning to meet their responsibilities. Our emphasis is on taking proactive measures to make sure the vast public funds involved are properly expended and utilized. At this time, there are still questions and implementation issues that need to be explored and resolved with respect to how the relevant oversight bodies involved—IGs, Government Accountability Office (GAO), and the Board—can best work together to perform the rigorous oversight desired by Congress and the public. As requested by the Committee, my testimony today will address the new responsibilities imposed by the Recovery Act on IGs; the IG community's current stimulus oversight activities; USDA OIG's oversight plans for the Recovery Act funds that support USDA stimulus activities; and some "lessons learned" from the community with respect to supplemental appropriations for expedited Federal programs and operations.

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<sup>1</sup> H.R. 1, Public Law 111-5, February 17, 2009.

## **I. New IG Responsibilities Pursuant to the Recovery Act**

The Recovery Act creates new responsibilities for Federal IGs in three main areas: oversight of agency stimulus-funded programs, participation on the new oversight accountability board, and investigations of whistleblower complaints. My testimony will discuss some of the most challenging elements of these new responsibilities for the IG community.

### *1. Oversight of Stimulus Expenditures*

Under the IG Act, IGs generally have broad oversight responsibility and authority for their parent entities' programs and operations. Recovery Act-funded activities at each Federal entity have become significant additions to this portfolio. IGs are giving high priority to oversight of stimulus activities due to the Act's requirements for mandatory reviews, investigations, reports, and—most importantly—the joint governmental and public interest in ensuring that expedited stimulus funds are spent properly. Agencies must promptly develop plans for allocating stimulus funds, including identifying and assessing any risks regarding the responsible disbursement and ultimate usage of the monies involved and appropriate risk mitigation strategies. IGs must also report on funds spent on our oversight activities.

Section 1514 of the Act mandates that an IG shall review, as appropriate, any concerns raised by the public about specific investments of stimulus funds. Unless criminal proceedings are involved, the OIG must relay its findings immediately to the agency head and post them on the OIG's web site (subject to privacy laws). The Recovery Act also provides new authority to OIGs to examine records and interview the employees of entities that receive stimulus funds. At this time, the volume and substance of the public complaints individual IGs will receive regarding stimulus activities—and the level of OIG resources required to address them—is difficult to predict. It is certainly an element of the Recovery Act, however, that the IG community must plan for and closely monitor.

*2. The Recovery Accountability and Transparency Board*

The Recovery Act creates a new Recovery Accountability and Transparency Board to coordinate and conduct oversight of stimulus programs. The Board is comprised of 10 IGs and is chaired by the Honorable Earl Devaney, IG at the Department of Interior. The Board has a number of functions, and is required to coordinate its work with individual IGs and the Council to avoid duplication of effort. Congress provided the Board with extensive audit and program review powers, but not investigative authority; allegations requiring investigations of a criminal nature must be referred to the appropriate OIG. The authorization for the Board expires on September 30, 2013.

During the Recovery Act's legislative development, there was extensive discussion in the IG community about the potential impact of the Board on OIG activities, such as whether unintended difficulties or interference with traditional IG independence and responsibilities would occur. We appreciate the assistance rendered by Committee Members in removing or modifying various provisions that were of concern regarding IG independence and the potential for conflict between the Board and IGs. In particular, we note that all of the Board's members are now IGs, a highly experienced IG has been appointed as Chairman, the Recovery Act clearly provides that each IG makes the final decision on audits and investigations to be pursued, and the Board and the Council are required to coordinate their activities. I therefore anticipate that the IG community will be able to forge a productive working relationship with the Board as it takes up its oversight responsibilities.

*3. Assessing Whistleblower Complaints Related to Stimulus Activities*

The third element of the Recovery Act that may significantly impact the IG community is the new protections from reprisal provided to whistleblowers who are State and local government employees or contractors. When such individuals present Federal officials with information they believe is evidence of gross mismanagement, waste, or illegality related to stimulus

expenditures, IGs are required to investigate any reprisal complaints that may result.<sup>2</sup> IGs are required to complete these whistleblower investigations within 180 days, subject to certain extensions. The Act's whistleblower mandates present a broad new area of potentially substantial investigative obligations for IGs regarding non-Federal employees and contractors. At this time, it is too early to predict the administrative and budgetary effects of these requirements as stimulus funds flow to States and localities. As the IG community gains experience over the course of the Act in meeting the whistleblower mandates, we will keep the Committee informed should any substantive procedural or resource allocation concerns arise.

## **II. Initial IG Community Actions in Response to the Recovery Act**

### *The Council of Inspectors General on Integrity and Efficiency*

Due in large part to the efforts and legislative determination of Members of this Committee, the Inspector General Reform Act of 2008<sup>3</sup> created the Council of Inspectors General on Integrity and Efficiency (Council) which is comprised of Federal IGs and senior-level Federal officials from the Federal Bureau of Investigation, Office of Government Ethics, and Office of Special Counsel, among other entities. The Deputy Director for Management of the Office of Management and Budget (OMB) serves as the Executive Chair of the Council, and I am privileged to have been elected as the IG that serves as Chair of the Council for the next 2 years. Among the functions and duties stipulated by Congress for the Council are identifying and reviewing areas of weakness and vulnerability in Federal programs with respect to fraud and mismanagement and developing plans for coordinated Governmentwide activities that address such problems and promote efficiency in Federal programs and operations.

While each IG has unique challenges based on the nature of his/her agency's programs, a core purpose and value of the Council is to facilitate prompt information sharing between IGs about varying oversight approaches and experiences. A priority for me as Council Chair during the Recovery Act's implementation will be to continually explore effective, common

<sup>2</sup> The Act provides exemptions for OIGs to decline to initiate an investigation in circumstances of frivolous complaints, concurrent administrative/judicial proceedings, and lack of connection to stimulus funds, among others.

<sup>3</sup> Public Law 110-409, October 14, 2008.



oversight approaches among IGs, and for our community to emphasize preventive measures that can be taken before public funds are expended.

*IG Community Coordination with OMB and GAO on the Recovery Act*

As part of our efforts, the Council worked with OMB to provide input on OMB's draft implementing guidance to agencies for their Recovery Act activities. The guidance contains critical steps that Federal agencies must immediately take to meet the objectives of transparency and accountability for Recovery Act monies. The Council's comments to OMB generally sought to enhance and fine tune the guidance's oversight requirements and more clearly distinguish the role of IGs from that of the managers of the programs being funded by the Recovery Act. Among the noteworthy changes recommended by CIGIE and adopted by OMB were: (1) extending the Federal Acquisition Regulation rule regarding "self-reporting" of fraud by contractors to Recovery Act grantees and loan recipients; (2) requiring agencies to expedite any corrective actions necessary for weaknesses and deficiencies that have been disclosed by prior audits and investigations and are relevant to imminent Recovery Act activities; and (3) providing that agency web sites have recovery program pages that link directly to their OIG web pages so that the public can contact OIGs directly about concerns related to stimulus programs. The Council and I will continue to work closely with OMB as it issues additional implementation guidance concerning the stimulus funds received and disbursed by Federal agencies.

With respect to IG coordination with GAO, I believe that most OIGs have excellent working relationships with their GAO counterparts in carrying out oversight activities. This is certainly the case for my agency, USDA OIG; we work very closely and productively with the GAO staff involved in agriculture, nutrition, and natural resources issues. These relationships have been built over many years, as the IG Act requires IGs to coordinate with GAO to reduce potential duplication in our respective audits and program reviews.

The IG Stimulus Working Group (discussed below) recently met with Acting Comptroller General Gene Dodaro and senior GAO officials to discuss community approaches to meeting

our new responsibilities under the Recovery Act. One issue of paramount concern to all is the need to ensure that stimulus funds are properly spent as they flow from Federal agencies to the State and local levels. There is general recognition that the traditional oversight provided by the Single Audit Act and OMB Circular A-133 will not be sufficient to provide timely and effective feedback on stimulus programs this year. While non-Federal entities are required to have an annual audit of their Federal awards and funds, the results are not available until at least 9 months after their fiscal years end. It is therefore necessary for the Federal oversight community to develop more timely approaches to overseeing the massive flow of money to State and local entities. IGs whose agencies have significant program dollars going to non-Federal recipients have already started to reach out to their State and local counterparts and to perform risk analyses of those programs to determine the types of testing that should be done. We also understand that GAO will be working closely with these governments to follow the flow of program funds and to ensure that these entities report their activities in a timely and consistent way. As IGs, we will need to coordinate our own reviews of program effectiveness closely with GAO to ensure that there are no gaps in our coverage. We believe that this is an opportunity for further productive collaboration between the IG community and GAO.<sup>4</sup>

*Sharing Oversight "Best Practices": The Stimulus Oversight Working Group*

The Council has created a Stimulus Oversight Working Group comprised of the 23 IGs whose parent agencies are receiving Recovery Act funds. I believe this Stimulus Working Group can serve as an excellent forum for IGs directly responsible for stimulus oversight to discuss and share strategies, best practices, and other proactive measures to provide rigorous oversight of stimulus activities. The Stimulus Working Group recently held its first meeting to discuss common concerns and oversight practices being implemented community-wide. I would like to present the Committee with an overview of the information these IGs have provided about their Recovery Act oversight planning.

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<sup>4</sup> The related issue of OIG liaison with State and local audit entities is further discussed in Section V of this statement.

### III. Proactive Measures: IG Community Plans for Recovery Act Oversight

To inform the Committee about the specific stimulus oversight measures currently being considered or utilized, my office surveyed the IGs participating in the Stimulus Oversight Working Group. We asked these OIGs to provide brief responses on three aspects of their planning regarding the Recovery Act programs and operations under their jurisdiction. They were (a) provide examples of preventive and proactive stimulus oversight measures that the OIG is taking at this time; (b) provide examples of longer term stimulus oversight measures being planned; and (c) identify challenges the OIG faces in implementing its stimulus oversight activities. Below is a summary of some of the measures that are actively being implemented or considered by various Working Group IGs and some of the challenges noted by a number of the respondents.<sup>5</sup>

#### A. Preventive and Proactive Measures Being Taken Now

##### *Communicating with Senior Managers at the OIG's Parent Agency/Department*

- Establish Recovery Act steering committees (or partner with) agency officials regarding oversight activities and reporting.
- Evaluate agency stimulus spending, implementation plans, and performance measures.
- Evaluate unimplemented recommendations and provide technical advice, best practices, and guidance to agencies in areas targeted for stimulus spending.

##### *Heightening Fraud Awareness in Recovery Act Assistance Programs*

- Provide fraud awareness briefings and training to grant administrators and grantees.
- Determine what the agencies and program administrators are doing to reduce the risk of fraud, waste, error, and misuse relevant to stimulus activities.

##### *Reviewing Loan, Grant, and Contract Activities*

- Monitor grant planning activities and conduct pre-award audits of recipients.
- Prioritize audit efforts based on existing program risks and amount of supplemental stimulus funding.
- Adjust in process OIG audits (such as expanding/expediting them) to monitor supplemental funding.

<sup>5</sup> Each IG has the authority to determine his/her own respective oversight plans and actions and can best respond to inquiries about the details and status of their particular Recovery Act activities.

### **B. Longer-Term Oversight Measures**

- Obtain the appropriate level of additional audit and investigative staff via hiring, temporary employees, and the use of contract personnel.
- Develop and implement risk-based audit and investigation plans for stimulus funded grants, contracts, and agency programs and their respective financial management systems.
- Initiate criminal investigations based on Hotline complaints, agency referrals, audit work, and other sources.
- Conduct outreach to the external audit community (CPAs and State and local audit agencies) to provide technical assistance for their required audit oversight.
- Utilize data analysis and data matching to target programs receiving Recovery Act funding to look at eligibility issues and identify potential fraud, etc.
- Track agencies' compliance with the transparency requirements of the Recovery Act and verify data quality reports issued by agencies and posted to "Recovery.gov"

### **C. Challenges Facing OIGs for Recovery Act Oversight**

- Meeting the oversight requirements of the Recovery Act while continuing to conduct other statutorily mandated and high-profile work such as Federal Information Security Management Act (FISMA), financial statement audits, and unscheduled congressional and agency requests.
- Meeting staffing needs, training new hires, and obtaining contractor assistance with experience in the targeted program areas.
- Ensuring that funds passed to State and local governments are adequately tracked.
- The inability to perform timely computer data matching across Federal agencies.
- Ensuring timely reporting of audit, inspection, and investigative issues.
- Identifying and monitoring critical Information Technology systems that are used to provide transparency.
- Monitoring agencies' internal control structures and timing audits when funds are being disbursed.

#### IV. USDA OIG's Preliminary Oversight Plan for USDA's Stimulus Activities

While I am increasingly engaged in Governmentwide oversight issues and organizations on behalf of the Council and the Oversight Board, my primary responsibility is my service as IG at the Department of Agriculture. USDA OIG is directly responsible for continuous oversight of USDA's vast programs and operations; in fiscal year 2008, the Department had expenditures of approximately \$95 billion and approximately 90,000 full-time employees. USDA alone received \$28 billion in Recovery Act funding for a broad array of Department programs and operation, ranging from rural development programs, nutrition assistance, and watershed activities, to wildfire management and broadband activities. Nine separate USDA programs or accounts received at least \$300 million in supplemental funding, and the Supplemental Nutrition Assistance Program (SNAP)—formerly known as the Food Stamp Program—received \$20.1 billion for increased benefits and administrative expenses. The major new program expenditures at USDA utilizing Recovery Act funds will present significant oversight challenges for our OIG.

We have developed a number of actions to enable OIG to provide timely and effective oversight of USDA's Recovery Act expenditures. Our oversight plan is of course preliminary, since we will regularly make adjustments and shift our resources as the numerous USDA program agencies involved develop their own plans for stimulus activities and begin to spend the monies.

In addition to the efforts described below, we are conducting immediate outreach to the Department—including meetings with the top officials of the relevant USDA agencies—to advise them of OIG's plans and to solicit their input on where our efforts would be most effective. We are providing them with information on oversight "best practices" as they come to our attention. For example, we have already provided USDA agencies with a recently issued guide to grant oversight and best practices for combating grant fraud. Summarized below are the major elements of our preliminary USDA OIG oversight plan, organized by audit and investigative activity.

**A. Recovery Act Oversight at USDA: Audits**

We will focus on key elements such as whether USDA agency officials have established proper internal control procedures and compliance operations, as well as review whether participants in stimulus-related programs meet eligibility guidelines. OIG's audit work will be conducted in multiple phases based on USDA's Recovery Act activities and expenditures.

**Phase 1:**

- (1) In recent years, OIG has made audit recommendations on virtually every USDA program that will receive stimulus funding. We are now assessing the extent to which USDA agencies have implemented our recommendations to determine whether program weaknesses have been corrected. In cases where OIG's recommendations were not agreed-to or not fully implemented, we will work with agency officials to identify the corrective actions necessary to ensure effective controls on USDA's Recovery Act expenditures.
- (2) We are also considering expanding the scope of audits that are already in process or planned for USDA programs receiving stimulus funds. Among them are reviews of Farm Service Agency oversight of farm loans; Rural Development (RD) programs for single family housing, business/industry loans, and water and waste disposal programs; the Forest Service's wildland firefighting program; and the Food and Nutrition Service's SNAP program.
- (3) We are expediting the completion and release of several audits related to Recovery Act-funded programs, including RD's broadband program and the rehabilitation of flood control dams by the Natural Resource Conservation Service.

**Phase 2:**

- (1) We will design new audits to specifically review various aspects of the programs receiving stimulus funding.

(2) We will review each USDA agency's Recovery Program Plan and then develop targeted oversight initiatives.

(3) Our newly formed Data Analysis and Data Mining group will begin its stimulus related oversight by analyzing data pertaining to RD's Direct Single Family Housing Loan Program.

**Phase 3:**

We will evaluate the determinations USDA agencies make about the effectiveness of their stimulus activities by analyzing their performance measures with respect to outcomes.

**B. Recovery Act Oversight at USDA: Investigations**

Our investigative efforts for the Recovery Act will emphasize preventing and identifying fraud; initiating timely investigations when potential criminal activity occurs; and responding to the new sources of whistleblower complaints according to the Act's benchmarks. Thereafter, Investigations will work with U.S. Attorneys and States Attorney General Offices to prosecute violators and seek asset forfeiture when appropriate.

**Phase 1:**

(1) OIG agents will increase the fraud awareness briefings we conduct for agency personnel and distribute information to program stakeholders on our investigative capabilities and the avenues available for citizens to report stimulus-related fraud. OIG fraud alert memoranda to USDA agency personnel will highlight fraud schemes attempted in other Federal entities to raise awareness levels.

(2) Our National Computer Forensic Division will assist in fraud identification related to USDA's stimulus programs, such as matching our audit data mining results against external data bases.

- (3) We will actively participate on national and regional task forces such as the Contract and Procurement Task Forces and the Mortgage Fraud Task Forces. These organizations increase OIG's ability to identify fraud and partner with other Federal/State investigators and prosecutors.
- (4) OIG will continue close liaison with USDA agencies to identify fraudulent activities and coordinate with their compliance and investigations units for joint investigations, as appropriate.
- (5) We will use OIG's Hotline as a source of information on potential criminal activity affecting USDA's stimulus activities. Each month, our Hotline staff receives approximately 275 contacts and performs an initial assessment of the complaints and allegations to determine the level of OIG investigative inquiry that is warranted. OIG will separately track complaints regarding Recovery Act funding and related whistleblower reprisal complaints.

**Phase 2:**

- (1) After assessing the results of the initiatives described above (and information revealed by our stimulus-related audit work), we will open criminal investigations as appropriate. Based on our experiences with emergency/supplemental USDA funds provided for Gulf Coast hurricane relief activities, we anticipate significant investigative work involving SNAP fraud.
- (2) Upon assessing our investigative results for USDA's stimulus activities, we will work to ensure that entities involved in criminal or serious misconduct are held accountable via criminal and/or civil prosecution, asset forfeiture, agency fines, and administrative sanctions (suspension/debarments, etc.).



**Reporting OIG's Recovery Act Activities and Results**

The closing comment I would like to offer regarding our preliminary oversight plan at USDA OIG pertains to our recognition of the importance of timely reporting by IGs about stimulus-related activities. Fulfilling our reporting obligations under the Recovery Act will assist agency heads and congressional oversight committees in carrying out their responsibilities. We will alert USDA officials to program integrity and efficiency problems as quickly as possible to expedite corrective actions. We will incorporate the Recovery Act's new requirements regarding whistleblower complaints into our semi-annual reports to Congress. As provided by OMB guidance, OIG will separately report our use of Recovery Act monies and other funds for stimulus-related activities in our reports and "Recovery.gov" submissions.

**V. Lessons Learned: Past OIG Oversight of Expedited Federal Expenditures**

As requested by the Committee, I will discuss the IG community's experiences from past oversight of Federal expenditures. While the amount and scope of the Recovery Act's expenditures are unprecedented, the multi-agency, expedited nature of the Federal response to Hurricane Katrina resulted in important "lessons learned" for IGs and program officials that could apply to stimulus-funded activities.

Critical to the successful performance of the IG community in providing effective oversight of Hurricane Katrina response activity was the systematic coordination and utilization of the skills, resources, and experience of a broad array of OIGs. Led by the Department of Homeland Security's (DHS) OIG, those OIGs whose agencies were involved in the hurricane recovery efforts established an oversight plan for mitigating crisis procurement risks, managing the broad scope of oversight work, and overseeing contracts. The OIGs refined the plan into an audit coordination model that outlined which offices would focus on specific Federal activities during the different phases of recovery efforts. Audit personnel from nine OIGs formed a Hurricane Katrina Contract Audit Task Force to coordinate efforts. The IG community also developed an investigation coordination model to address how case referrals and investigations would be managed.

The IGs involved in Katrina recovery oversight also coordinated their efforts with other law enforcement agencies to ensure that criminal activity was investigated and prosecuted. The Department of Justice created a Hurricane Katrina Fraud Task to investigate, prosecute, and deter fraud from any domestic natural/manmade disaster.<sup>6</sup> According to DHS OIG, the task force command center referred 21,000 complaints to law enforcement and brought Federal charges against more than 900. On the audit side of the community, OIGs providing Katrina-relief oversight completed more than 150 audits that resulted in substantial monetary results (questioned and unallowable costs, etc.) for the Government and taxpayers.<sup>7</sup>

The IG community provided a complete discussion of our lessons learned from the Gulf Coast hurricanes in an October 2006 report to Congress.<sup>8</sup> For the purposes of today's hearing, I will briefly highlight some of the more significant elements my colleagues compiled for the Committee as you begin to explore effective oversight practices for the Recovery Act.

✓ ***Efficacy of Risk Management Activities***

IGs have found that programs that have existing problems managing risk in their grant and procurement processes will experience significant deficiencies in effectiveness when they try to manage and spend large increases in funds in a short period of time. The staffing and infrastructure of these programs are not equipped to properly manage rapid and large funding increases. OIGs should review agency risk management activities and internal controls relevant to the management of the Recovery Act's supplemental and expedited funding.

✓ ***State and Local Liaison***

The Committee has aptly expressed an interest in the accountability of funds as they flow from the Federal to State and local entities. The Recovery Act brings increased challenges to Federal IGs to oversee the flow of funds at the Federal level (through the awards of contracts, grants, loans, etc.) and then to follow the funds as they flow to the State and local levels. Similar to Gulf Coast hurricane relief measures, a large portion of the Recovery Act's funding

<sup>6</sup> Based in Baton Rouge, Louisiana, it is now known as the National Center for Disaster Fraud. More than 20 Federal agencies are located at the command center.

<sup>7</sup> For example, DHS-OIG reported \$197 million in questioned costs pertaining to hurricane relief activities through FY 2008.

<sup>8</sup> The President's Council on Integrity and Efficiency – *Oversight of Gulf Coast Hurricane Recovery: A Semiannual Report to Congress, October 2006*.

will be passed through State and local governments. Proactive and continuing communication and coordination between IGs, GAO, and the Board with State and local audit communities is vital. Developing audit response plans with state and local audit partners has proven effective for Federal IGs. Resource-draining duplication must be avoided to the greatest extent possible.<sup>9</sup>

✓ **Information Data Sharing**

Interagency data sharing and coordination is important when funds are spent in interagency efforts. However, Federal law on agency computer matching limits the ability of IGs to promptly share data.<sup>10</sup> The IG community certainly recognizes the importance of computer matching safeguards, but a number of OIGs have found that current restrictions hampered past efforts to prevent and pursue fraud. Members of the Council have discussed the concern that the absence of computer matching agreements forced the Hurricane Katrina Fraud Task Force to rely on manual record searches to detect improper payments and fraud. The problem identified was that IG oversight practices can encounter delays and obstacles due to the need to gain cooperation from the managers of agency database systems. Members of the Council have discussed this concern with Committee staff and welcome further consideration of this issue.

✓ **Training**

Part of the Council's mission is to ensure that IG community oversight personnel are properly trained, and a lesson from the Katrina relief effort was that OIG personnel may need advanced training in specialized programs. Members of the community will need to evaluate the particularized training needs of their offices as they assess the audit and investigative oversight required for Recovery Act activities.

<sup>9</sup> See the related discussion of IG and GAO stimulus oversight involving State and local entities in Section II.

<sup>10</sup> The Computer Matching and Privacy Protection Act of 1988, Public Law 100-503.

✓ **Staffing**

In working to provide OIG staff necessary for the audits and investigations desired for expedited Recovery Act activities, IG managers must be mindful to maintain the proper level of continuing oversight for their parent agencies or Departments' recurring programs and operations.

This concludes my testimony. I want to thank the Committee for the opportunity to share my views and those of the IG community on these issues. I would be pleased to address your questions.

**STATEMENT OF  
DR. ALLAN V. BURMAN  
PRESIDENT, JEFFERSON SOLUTIONS,  
a Division of  
JEFFERSON CONSULTING GROUP, LLC  
BEFORE THE  
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
MARCH 5, 2009**

Mr. Chairman,

I very much appreciate the opportunity to provide this statement to you, Senator Collins and the other members of the Committee regarding contracting issues and the use of American Recovery and Reinvestment Act (ARRA) funds. I am a former Administrator for Federal Procurement Policy (OFPP) in the Office of Management and Budget (OMB), acting in that position under President Reagan, confirmed by the Senate under President George H.W. Bush and then staying on in that role under President Clinton.

As Administrator, I was charged with setting guidelines for carrying out government acquisitions and many of the policies I initiated remain in effect today. These include those requiring the use of past performance and performance-based contracting techniques as well as the government's approach for defining inherently governmental functions.

Since joining the Jefferson Consulting Group in 1994, I have led the firm's government consulting practice in which we provide acquisition training and management consulting to a variety of agencies across the government as well as overseas. I also recently served as a member of the Congressionally chartered Acquisition Advisory Panel that in 2007 provided its report to OFPP and the Congress on ways to improve services contracting. I teach government contracting as an adjunct professor for George Mason University as well as for the International Law Institute.

I appreciate the importance and breadth of actions required to put the Stimulus program into effect and to provide effective oversight. The initial implementing guidance on ARRA released February 18, 2009 by OMB Director Orszag is thorough and sound. I very much applaud the efforts to make this process as successful, fair and transparent as possible for the American people.

While there are many important issues to be addressed, I will confine my remarks specifically to the contracting challenges associated with putting the program in place. I would particularly like to call the Committee's attention to the need for agencies to be fully prepared to define requirements and desired results early in the planning process, and to have sufficient and well-qualified acquisition resources in place to manage the procurements in a timely and effective manner.

In its implementation guidance, OMB lays out special requirements for contracting under ARRA. Having spent many years at OMB, I have great respect for that organization and I am sure that OFPP will do all they can to help agencies move this program forward. Key provisions of the guidance focus on maximizing opportunities for small business, streamlining award processes and maximizing competition, all worthy goals. Agencies are asked to do the following:

- Define contract requirements that deliver meaningful and measurable outcomes consistent with agency plans and the goals of the Recovery Act
- Obtain maximum practicable competition and clearly report contracts where competition was not used
- Apply sufficient and adequately trained workforce to responsibly plan, evaluate, award and monitor contracts
- Ensure an adequate number of qualified governmental personnel are available to perform inherently governmental functions
- Provide appropriate agency oversight at critical decision points

In carrying out these steps, agencies are encouraged whenever possible to use fixed-price contracts. One reason for this preference is that this contract type requires the contractor not the government to accept the risk of getting the job done. However, in order for contractors to be able to propose thorough and complete solutions and an accurate firm fixed price, it is essential that the government accurately define its requirements and objectives.

The guidelines also offer ways to try to obtain necessary staffing to see that the contracting process is done effectively, since standard procedures are to be followed in putting these awards in place. This is critical, given that there is a broad consensus that the acquisition process is currently facing a number of relevant and serious challenges.

Over the last year I have been engaged with a number of thought leaders through a program sponsored by George Mason University and IBM's Center for the Business of Government in assessing the acquisition processes of the Federal government. The conclusion from that assessment raises several critical concerns:

- Contracting staffing has remained relatively level at approximately 60,000 people since 2000 while the dollars associated with contracting have almost doubled to \$470 billion in 2007. This total comprises almost 40 percent of all discretionary spending by agencies. Not only are contracting staff managing a much higher procurement volume, but as agencies have moved toward acquiring services and solutions rather than commodities, procurement complexity has also significantly increased.
- Federal agencies are critically dependent on an effective acquisition process to accomplish their missions, yet many observers feel the system is broken, mired in cost overruns, accountability lapses and questionable outcomes.
- Those operating within the system see the environment as "toxic", characterized by fear and mistrust, with oversight bodies such as Inspectors General second-guessing their every action.

Our Acquisition Advisory Committee report cited similar concerns, and particularly the pressure on the acquisition community of “getting to award”, with little time for the necessary responsibilities associated with seeing that the government is actually getting what it is paying for. But even more problematic was the difficulty that every agency is experiencing in being able to adequately define requirements at the beginning of the contracting process. Numerous Government Accountability Office (GAO) and Inspector General reports cite as the key reason for failure of procurements the inability of the government to get the requirements right up front in the process. This was a message that our Panel heard from both government staff and contractors alike.

This problem is compounded by the difficulties in achieving effective collaboration between the agency contracting office staff responsible for putting the contract in place and the program staff that has the responsibility for both defining what is being sought and then monitoring contractor activities to see that the results are achieved. One of the biggest challenges in moving toward a performance-based environment is in seeing that the right people work together as a team and ensure that all of these responsibilities are successfully met over the life of the contract.

These issues are very real. Just last month I met with contracting staff as part of a larger acquisition review project. In an office that is still finishing one-quarter of its work from last year, to accomplish the goals of ARRA, they are expecting to have 17 years of work to do in the next few months without any sizeable increase in staff.

These problems may be even more pronounced in state agencies and those in counties and cities across the country that are strapped for funds and training. Many locations expecting millions of dollars in Stimulus money will be challenged to contract with firms who can do the work and create the jobs this legislation was designed to do. These communities may want to consider using the General Services Administration schedules program where available to them as a proven vehicle that is easy to use and reduces the risks associated with rapid timelines and high volume procurement.

It is critical that agencies proactively address these issues. We have seen from the experiences in Iraq and Katrina the consequences of pressure to get to award but then the after-effects as reviewers point out all the flaws of what was done and what was not done. To have these funds distributed poorly or wastefully in spite of the best intentions of all involved will benefit no one and only serve to call into question the basic integrity of the whole procurement process.

There are actions that can be taken now that will help ensure the Nation gets the best results possible through its contracting efforts in the ARRA program. I offer the Committee the following suggestions:

- Agencies should see that contracting staff and program officials are collaborating effectively at the front end of the process both in defining requirements and putting in place an effective monitoring approach to ensure results are achieved.

Our George Mason – IBM working group identified the Chief Acquisition Officer, a position established by Congress, as the likely position to see that this collaboration takes place. However, since these are non-career positions, many of them may not yet have been filled. Moreover, many agencies have not used this position effectively, assigning this responsibility to individuals not adequately qualified to carry it out or having so many other responsibilities that they cannot give reasonable attention to the role. Agencies should assign a key senior official the role to ask these important questions regarding up front collaboration and make sure contracting actions are aligned with agency and Congressional intent.

- Encourage, or direct, agencies to use an independent review body such as the National Academy of Public Administration to serve as an independent check to see that this collaboration is both working and effective at the front end of the process, before the contracts are let, as well as during the contract life. This is a role that the Academy is well equipped to play and Congress in the past has frequently suggested that agencies look to the Academy for this type of sound, objective management guidance and assistance. We all recognize the pressures that will be on contracting staff to get these funds out quickly so that they are working effectively for the American people. Having someone outside the agency providing guidance and concurrently providing a check to see that acquisition planning and execution are done well will prevent all kinds of problems later on. The Academy could assist in developing government-wide templates and in seeing that good practices by one agency are made available to others as well. This would not be a post-mortem review body ready to criticize poor performance but rather a proactive partner to help make good performance the rule and not the exception.
- Establish a business council at each civilian agency chaired by the Deputy Secretary with membership of the agency chief management officials, including Chief Acquisition Officer, Chief Information Officer, Chief Financial Officer and Chief Human Capital Officer to focus directly on all of the major agency contracting efforts. Such a body will offer another means of ensuring that effective business type collaboration is occurring at the highest level of the agency to define requirements and desired outcomes and the acquisition process is aligned with agency objectives.
- Consider creating a Federal “contracting life line” that states and localities might use for online training of staff and for acquiring effective templates and best practice approaches for seeing that they get the best possible results from their contracting efforts.

The George Mason–IBM assessment resulted in a number of other long-term recommendations that would also significantly improve the acquisition process. These include the following:



- Initiating a more robust human capital strategic planning process that would provide a full picture of all federal and contractor resources likely to be needed to accomplish agency missions.
- Providing sufficient resources to see that the right people with the right talent are in place to carry out all aspects of the acquisition function; as this Committee recommended, the Congress in the National Defense Authorization Act for 2009 has already taken steps to address acquisition workforce issues in terms of better defining staffing needs and addressing the issue of what constitute inherently governmental functions. These will be important efforts in seeing that agencies conduct effective human capital strategic planning to meet the acquisition challenges described above.
- Transform OFPP into an Office of Federal Acquisition Policy and include agency program managers under its policy purview to help to bring about that collaboration between program and contracting staff critical to an effective acquisition process.

Mr. Chairman, thank you and Senator Collins again for this opportunity to provide my views on these important issues.

**Post-Hearing Questions for the Record  
Submitted to the Honorable Robert L. Nabors II  
From Senator Mark L. Pryor**

**“Follow the Money: Transparency and Accountability for Recovery and  
Reinvestment Spending”  
March 5, 2009**

1. *What will be the process for agency IGs, GAO, and OMB to get together to “compare notes” and discuss big-picture oversight of the Recovery Act funds? How often will representatives of these agencies meet?*

**Response:**

Ongoing collaboration between OMB, GAO, and the Inspector General community has been underway since the Act was passed in mid-February, with almost daily communication among OMB, the Recovery Board, GAO, and the Council of Inspectors General on Integrity and Efficiency (CIGIE). Notable collaborative efforts to date include:

- OMB and the Recovery Board are partnering in our efforts to implement the data reporting requirements of the Recovery Act. The Board has provided critical input into OMB guidance on data reporting requirements and OMB, in turn, is supporting the Board’s efforts to develop and implement data reporting solutions.
- OMB and GAO jointly host a weekly meeting with representatives of key State associations (e.g., the National Governors Association, the National Conference of State Legislators, the National Association of State Auditors, Comptrollers, and Treasurers) to discuss Recovery Act implementation challenges and appropriate solutions.
- OMB shared early and multiple drafts of OMB implementation guidance (M-09-10 and M-09-15) with the CIGIE, obtaining useful feedback that was incorporated into materials before they were finalized.

OMB will continue to explore ways to enhance collaborative efforts among and within these organizations to ensure that we share common objectives and find workable solutions to Recovery Act implementation challenges.

2. *Federal law already requires that the government provide details on federal contracting and grant expenditures through USASpending.gov.*
  - a) *Will the recipients of stimulus funds, including state and local agencies and the contractors and subcontractors working for those agencies, be required to report on the use of these funds to this website in addition to [www.Recovery.gov](http://www.Recovery.gov)?*

**Response:** Recipients of stimulus funds will not be required to report to USASpending.gov in addition to Recovery.gov. OMB is working closely with the Recovery Accountability and Transparency Board to ensure any data collection

efforts are closely coordinated and do not impose overlapping burdens on the recipients of Federal funding.

Of note, Federal agencies will continue to report information required by the Federal Funding Accountability and Transparency Act (FFATA) on payments to recipients. We have modified the FFATA reporting framework to identify payments to recipients made with Recovery Act dollars. The primary recipient of Federal Recovery dollars will report information required by Section 1512 of the Recovery Act on Recovery.gov. Included within Section 1512 is detailed information on projects and activities funded with Recovery dollars, including common data elements required under FFATA. Federal agencies will provide FFATA data on the primary recipient, and the primary recipient in turn will provide FFATA data on their sub-recipients. Thus, the reporting is complementary, not duplicative.

*b) What is the timeline for making this information available to the public?*

**Response:** Section 1512 of the Recovery Act requires recipient reporting to begin 180 days after enactment, and for reports to be submitted by recipients 10 days after the end of each calendar quarter and made public 30 days after the end of each calendar quarter. This results in an initial statutory reporting deadline of October 10, 2009, with the first reports made public by October 30, 2009.

*c) What definitions, forms, and standards for reporting this information to the public are being developed?*

**Response:** OMB issued general guidance to Federal agencies on April 3, 2009, explaining how the information required by Section 1512 of the Recovery Act will be collected. This guidance also included the data elements for recipient reporting that were issued as changes to Federal regulations (the Federal Acquisition Regulations for contracts and Title 2 for grants and loans). Further, OMB published a Paperwork Reduction Act notice in the Federal Register on April 1, 2009, providing additional detail on Section 1512 reporting requirements. OMB and the Recovery Accountability and Transparency Board are currently developing additional guidance on the process, data formats, and technology for collecting required information. We expect to issue this more detailed and technical guidance on the reporting solution in June.

#### **From Senator George V. Voinovich**

*1. How does OMB define a 'green-collar job'?*

The definition of green jobs is chiefly the responsibility of BLS and CEA. My understanding is that BLS is exploring options for how best to define and collect these data using modifications to existing surveys. The 2010 Budget includes \$8 million for the Bureau of Labor Statistics (BLS), the chief source of Federal Government data on jobs, to produce detailed, occupation-specific data on green jobs and classify green jobs as part of that effort.

**Homeland Security and Governmental Affairs Committee**  
**“Recovery and Investment Spending: Implementing a Bold Oversight Strategy”**  
 Chairman Joseph Lieberman  
 April 2, 2009

Good morning and welcome to this second in what will be a continuing series of hearings this Committee, pursuant to its oversight responsibilities, will hold to monitor how billions of taxpayers’ dollars are being spent under the American Recovery and Reinvestment Act.

To give you an idea of what we would like to accomplish with these hearings, I’d like to quote Benjamin Franklin who said: “It takes many good deeds to build a good reputation, and only one bad one to lose it.”

And so it is with the Recovery Act. Americans want the Recovery Act to succeed – need it to succeed so it can save or create 4 million jobs and get our economy growing again.

But if Americans start hearing stories about how their money being wasted on pet projects or funneled to favorite contractors or flat out lost to fraud or theft, faith in government at all levels and support for the overall program will erode – no matter that other parts of the program are successful. I understand that is a large undertaking: to say that we will prevent any waste and abuse, but that has got to be our goal.

We want to use these hearings – in cooperation with the Administration – as a way to spot potential problems and do what we can to solve them before they become financial scandals that hurt all Recovery Act programs.

To help with the very supervision I’m talking about, the Recovery Act created the Recovery Accountability and Transparency Board composed of a chairman and 10 inspectors general from across the federal government.

That board met for the first time last Friday and its chairman, Earl Devaney – on loan from his job as Inspector General of the Interior Department – joins us here today and we look forward to hearing how that first meeting went and what plans or recommendations may already be in place or emerging.

The Recovery Act also included \$250 million for federal inspectors general to hire additional experienced auditors and investigators for their agencies. This is good. But we need to remember that much of the nearly \$500 billion in spending will be contracted and supervised by state and local governments – governments whose budgets have been crippled by the recession.

For instance, my home state of Connecticut is facing spending cuts that may total \$2 billion over the next two years with layoffs almost guaranteed to be a part of that.

We need to talk about ways to help our states and municipalities retain and prepare the skilled managers, contract specialists and auditors they need to ensure this money is spent wisely and with accountability.

We need to make sure that State and local agencies – already stretched thin by this Great Recession – have the capacity to manage Recovery Act funds.

I want to note that our Committee will hold a field hearing Tuesday in my home state of Connecticut on this very challenge that our states and local governments face.

Also joining us is Rob Nabors the Deputy Director at the Office of Management and Budget. In addition to providing overall guidance to federal agencies on Recovery Act implementation, OMB has stood up the website, [recovery.gov](http://recovery.gov), which – if designed correctly – will allow journalists, bloggers and citizens to keep an eye on stimulus spending and report waste, fraud, abuse or theft if they suspect it.

I understand it's already getting about 4,000 hits a second.

This can be a marvelous tool not only to monitor Recovery Act spending, but could eventually help us develop powerful tools to monitor all federal spending.

But for it to work to its best potential, it will need to allow its users to burrow deep into the details of where and how and where the money is being spent and I want to follow up on concerns raised at our last hearing that the data trail may turn cold at the precise point spending needs to be monitored most closely – at the specific contract level.

I understand that Chairman Devaney's Board is taking over responsibility for content of Recovery.gov while OMB will remain responsible for the collection of data that feeds into the web site. I'd like to hear more from Mr. Nabors and Mr. Devaney about precise plans to make recovery.gov the incredibly useful fiscal watchdog tool I hope it can be.

Again, we ask these questions to spot the challenges ahead – the potential problems, flaws and loopholes – so we can prepare to meet them for as Ben Franklin also said: "By failing to prepare, you are preparing to fail."

And with our economy at stake, the American Recovery and Reinvestment Act – in the financial parlance of our time – is simply too big – and too important – to fail.

Senator Collins.

**Prepared Statement of  
Senator Susan M. Collins**

**'Recovery and Reinvestment Spending: Implementing a Bold Oversight  
Strategy'**

**April 2, 2009**

Nearly two months ago, the President signed into law the American Recovery and Reinvestment Act to help turn around our economy. Now the challenge is to make sure the billions of dollars provided by that law achieve the purpose of boosting our economy and saving and creating jobs.

As my Senate colleagues and I worked to craft this bill, we established an oversight board and imposed tough reporting requirements to help ensure transparency and accountability in the expenditure of the funds. We remain determined to protect this critical spending from waste, fraud and mismanagement.

Several provisions included in the law provide safeguards and oversight of stimulus spending. Perhaps most important is the Recovery Act Transparency Board, created to coordinate federal oversight efforts. The Government Accountability Office and many of our nation's Inspectors General also have been provided additional funding to carry out investigations and reporting requirements. A new website, [Recovery.gov](http://Recovery.gov), has been launched to report expenditures and to provide the public with access to stimulus information. The more eyes we have on this spending, the better.

The [Recovery.gov](http://Recovery.gov) website is now up and running and already has received 300 million hits. It now is linked to the individual Recovery Act websites for states and for federal agencies.

I have included a link to [Recovery.gov](http://Recovery.gov) from my own Senate website as well as a special website I created to provide Mainers with specific information about Recovery Act spending as it relates to our State. This technology not only allows an abundance of information to be shared quickly with people across the country, but also helps ensure transparency and accountability.

The American people have high expectations for the Recovery Act. The President has estimated that it will save or create approximately 3.5 million jobs and help turn the economy around. Taxpayer dollars will be used to improve roads and schools, enhance health care, and invest in infrastructure and science and must be spent wisely.

Funds need to be dispersed quickly to meet the goals of stimulating the economy, but we must ensure that haste does not make waste – or permit fraud and mismanagement. Striking the right balance between speed and caution will be difficult when administering the grants and contracts funded by the stimulus.

Press reports have already questioned whether the first few contracts awarded using stimulus funds were sufficiently transparent and whether contracting mistakes were made. This is not a reassuring start. Problems like these can easily erode public support and leave our economic goals unrealized.

Today's hearing will provide us with a more in-depth look at the most important oversight organization, the Recovery Accountability and Transparency Board. I look forward to hearing from Mr. Devaney, the Board's recently appointed Chairman.

From the Office of Management and Budget, I am particularly interested in hearing how it expects to address challenges in tracking funds at the state and local level, providing accurate and timely information on this spending on the Recovery.gov website, and ensuring transparency, accountability, and competition for stimulus contracting.

Our government has an obligation to make sure stimulus funds provide the maximum possible benefit to our economy. The American taxpayers deserve no less from their investment.



**Opening Statement: Sen. Tom Coburn**  
***Recovery and Reinvestment Spending: Implementing a Bold Oversight Strategy***  
**Homeland Security and Governmental Affairs Committee**  
**April 2, 2009**

Good morning, I would like to thank our witnesses for joining us at this hearing to discuss the implementation of the *American Recovery and Reinvestment Act of 2009* passed in February.

As most in this room know, I voted against the stimulus legislation because I strongly believe that adding \$787 billion to the national debt is not a wise strategy for reviving a stalled economy. While the legislation is well-intended, it relies on a theory that advocates huge increases in deficit spending as a means to pump money into the economy.

Unfortunately, it was irresponsible borrowing in both the public and private sectors that got us into a financial mess, and I do not believe that irresponsible borrowing will get us out.

That said, I believe firmly that an effort as large as the stimulus must be accompanied by an unprecedented level of transparency and accountability. I know that this is the goal of the President, who has spoken at length of his desire to see this money put to good use. When he was in the Senate, President Obama and I had the good fortune to develop legislation together that ultimately turned into USASpending.gov – a one-stop-shop website for taxpayers to see how their money is spent. Mr. Earl Devaney, head of the Recovery Act Accountability and Transparency Board, dubbed the RAT Board, said to the *Wall Street Journal* that, “We have to get in on the front end and try to prevent waste, fraud and abuse before it happens.” I agree, but in order to accomplish this, several problems need to be fixed.

First, the administration’s primary means of transparency, the Recovery.gov website, needs to be overhauled. I have personally tried to navigate the website and found it to be little more than a series of links to other agency webpages. My belief is that taxpayers will find it difficult to learn how their tax dollars are being spent.

It is understandable that there is little information on the website right now because little money has been spent on projects. Yet, a simple internet search finds hundreds of articles on stimulus projects all over the country that are either beginning or planned. Virtually none of this information can be found on Recovery.gov.

The average American was promised a website that provides one-stop-shopping for all stimulus spending and that is what they should get. Information should be easy to find and not buried in the bowels of an agency webpage. Without a major overhaul of the website, I am afraid that the American people will get an unprecedented level of confusion.

Second, Mr. Devaney said in the same *Wall Street Journal* interview that on average, seven percent of the money in a spending bill like this will be lost to fraud. That comes out to more than \$55 billion, which is more than \$1 billion per state.

Of course, if the government is operating at 93 percent efficiency, which Mr. Devaney’s numbers assume, it would be a record for government performance. It is likely that the fraud numbers will be much higher, costing tens of billions of dollars more. Either way, this is unacceptable.

Both of these issues are intrinsically linked – unless there is truly an unprecedented level of transparency there will be an unprecedented level of fraud.

I urge the administration to consider these issues carefully as we move forward with implementing the stimulus legislation.

**Testimony of Robert Nabors II**  
**Deputy Director, Office of Management and Budget**  
**Senate Homeland Security and Governmental Affairs Committee**  
**April 2, 2009**

Chairman Lieberman, Ranking Member Collins, distinguished Members of the Committee, thank you for inviting me to testify before you once again about the implementation of the American Recovery and Reinvestment Act.

Since I testified last month, the Administration has continued to advance the President's and Congress' commitment to move Recovery Act funds quickly and wisely, and with unprecedented levels of transparency and accountability to the public. We have also made strides in coordinating our efforts across all levels of government and in identifying and addressing the human capital needs created by this massive undertaking.

Today, I will talk about our progress in these key areas of Recovery Act implementation and the actions we have taken to address questions and concerns raised by this Committee last month.

**I will begin with an update on our recent efforts to spend Recovery Act funds quickly and effectively, and on the activities that are underway to ensure that spending continues over the coming weeks and months.**

Agencies are making steady progress in both announcing programs and obligating funds as quickly as possible. At the time of my last testimony, Medicaid accounted for almost all of the funds obligated. As of the end of March, Federal agencies had obligated over \$28 billion—nearly twice the amount as a month ago.

While just two agencies had issued notices of obligation at the beginning of March, an additional ten have done so in the interim. Most notably:

- The Department of Transportation (DOT) has obligated nearly \$4 billion for improvements to highways, transit, and railroads;
- The Department of Housing and Urban Development (HUD) has obligated more than \$4 billion for programs including Public Housing and Project-Based Rental Assistance; and
- The Department of Labor has obligated \$3.4 billion to support job training, services for dislocated workers, youth activities, and community service. The Department has also begun to obligate funds to States to modernize their unemployment insurance programs. In addition, recipients of unemployment insurance across States will now get an additional \$25 added to their checks every week.

In the case of Medicaid, States and territories have now drawn down about \$8.6 billion of the \$15.4 billion in Medicaid grant awards for the first two quarters of FY 2009—up from about \$3.3 billion a month ago.

In addition to obligations, there is other evidence of accelerating activity:

- Agencies have announced nearly \$151 billion in formula and block grants that will be made available to States. As these allocations enable States to foresee important increases to their budgets, they can influence State decision-making and benefit the economy even before they are technically obligated;
- Nearly 500 Recovery Act contracting opportunities, requests for information, and related notices are posted on the website “FedBizOpps”—and are easily identified through a search feature devoted specifically to the Recovery Act; and,
- 67 Recovery Act grant opportunities have been posted on Grants.gov, up from just ten last month. Current grant opportunities are valued at about \$23 billion.

To highlight some notable announcements, recipients of Social Security and Supplemental Security Income benefits can expect to receive \$250 Recovery Act payments beginning in early May and continuing throughout the month—which will inject over \$13 billion into the economy. And April 1 marked the deadline for employers to institute lower withholdings for their employees under the Making Work Pay tax credit—the tax reduction center piece of the Recovery Act.

**But it is insufficient to simply move money quickly. Therefore, the Administration is taking steps to spend Recovery Act funds with an unprecedented level of transparency and accountability.**

This remains a priority for the Administration, as well as for the American people, whose commitment to monitoring their government is apparent in the significant usage of Recovery.gov—which now has had a total of about 300 million hits, about twice as many hits as a month ago.

Speaking on behalf of OMB, I can tell you that our team is working extraordinarily hard to meet the accountability and transparency objectives of the Act. Although we have a heavy workload ahead, our progress over the past month has been significant. We have:

- Initiated the issuance of over 200 new, separate Treasury Appropriation Fund Symbols so Recovery dollars can be tracked and monitored separately;
- Reviewed numerous Federal agency spend plans to ensure that planned activities are prudent and well aligned with the programmatic and economic objectives of the Recovery Act;
- Worked closely with the Recovery Board to ensure a smooth transition of responsibility for Recovery.gov and to establish roles and responsibilities that ensure that OMB is best positioned to support the Board’s mission;
- Facilitated the launch of Recovery websites at all major agencies, all of which are accessible through Recovery.gov; and
- Made significant inroads in tracking and publicizing financial data.

On this last point, when I testified before you a month ago, agencies had just begun to submit weekly reports on the obligation and disbursement of funds, as well as block grant allocations and major communications and announcements—per the initial OMB guidance. Since then,

OMB has collected and reviewed incoming reports and worked extensively with the agencies to make them more comprehensive, as well as available to the public through Recovery.gov.

In response to input from this Committee, government officials at all levels, grant and contract recipients, and citizens, OMB is also taking further measures to clarify and enhance reporting requirements, and respond to developing needs for more data. In the next few days, we will be issuing an update to the initial guidance that we sent to the agencies on February 18. The update covers a broad range of areas, including program planning, data collection, and oversight.

Given the concerns expressed by this Committee about ensuring transparency for both primary and sub-recipients of funds, we have worked to expand our ability to drill down on specific projects or activities. The new guidance clarifies that for the approximately \$60 billion in Federal contract dollars under the Recovery Act, detailed information will be available on Federal contracts awarded, as well as subcontracts awarded from the prime contractor. Similarly, more than \$300 billion in grants are subject to recipient reporting requirements, and detailed information on the use of funds will be available on Federal grants awarded and sub-awards from the primary recipient.

To give you a sense of what this reporting system means in practical terms:

- Local organizations receiving the approximately \$85 billion in competitive awards will report on any sub-recipients that receive funds;
- For the approximately \$75 billion in Education grants, information will be available from both the State and the local school districts receiving funds;
- Local housing authorities will account for approximately \$8 billion in housing funds by reporting on any entities that receive funds from them; and
- For all of the approximately \$37 billion in highway and transit formula funding, grant recipients will be required to report on contractors they hire for various projects.

The Administration believes this level of reporting strikes the appropriate balance between transparency for Recovery Act spending and the burden that reporting imposes on recipients. But, ensuring transparency and accountability will remain an ongoing process, and OMB will continue taking proactive measures with respect to these priorities.

For example, in response to our discussion last month, I have asked OMB staff to work with the Government Accountability Office, Offices of Inspectors General, State auditors, and the American Institute of Certified Public Accountants to identify the best way to leverage the Single Audit process to maximize accountability and transparency for Recovery Act activities. By the end of April, OMB will publish an update to the Compliance Supplement for OMB Circular A-133 that will clarify the coverage of Single Audit for Recovery Act programs, highlight the significant accountability requirements for Recovery dollars, and help ensure that, when appropriate, Recovery programs are designated as high-risk and audited as “major programs.”

OMB plans to provide additional guidance to the auditors as more Recovery Act awards are made.

For FY 2009, the Annual Single Audits are now being conducted, covering initial Recovery Act activities. We are exploring the possibility of a review requirement that would provide early indicators of internal control breakdowns, requiring immediate corrective action. We believe we have general agreement from the audit community to partner Federal, State, and local audit resources in a coordinated manner that emphasizes the propriety of Recovery Act spending.

**This leads to another issue raised last month regarding the need to facilitate a partnership across levels of government in order to implement the Recovery Act successfully.**

We are working hard to maintain an open dialogue with stakeholders at the Federal, State, and local levels. The Vice President has spoken about Recovery Act implementation in at least ten separate venues across the country, including two meetings at the White House for State and local leaders. I have participated with the Vice President in some of these events, as well as in meetings with the National Governors Association, the National Council of State Legislatures, and the Urban League. With the specific goal of collecting feedback and fielding questions and answers, OMB holds weekly conference calls with groups representing State Auditors, Comptrollers, Treasurers, Chief Information Officers, and budget and procurement officials. Representatives from OMB have also participated in the National State Auditors Association Conference, the National Association of State Treasurers Conference, the National Association of Counties Conference, and the Association of Government Accountants Conference. OMB has held "town hall" meetings with representatives from agencies, States, and localities to provide technical assistance, share best-practices, and collect feedback. Just last week, we held a town hall to discuss a draft of the new guidance. All of these communications have helped us to craft our additional guidance in a way we believe will help States and localities implement the Recovery Act appropriately, effectively, and quickly.

In addition to communications surrounding guidance, OMB has extended outreach to States concerning the requirement that governors certify receipt of Recovery Act funds. Over the past weeks, we have worked closely with individual governors to make absolutely clear that they understand the boundaries of what can and cannot be done under the legal constraints of the Act. To date, all but three governors have certified. We have reached out to the governors' offices of the remaining three States to remind them of tomorrow's deadline for certification.

**To point to one other issue raised by members of this Committee, the Administration is committed to ensuring that agencies have the skills and capacity to plan effectively, award and administer contracts, and carry out programs funded by the Recovery Act.**

We are carefully reviewing a wide array of options to expand the capacity of agencies so they can meet the demands presented by the Recovery Act. Per the advice of this Committee, we are reviewing the use of a government-wide contingency contracting corps in limited circumstances. However, given the likelihood that the activities of the Recovery Act will require many agencies to handle an increased workload over an extended period of time, we are also encouraging

agencies to use various existing authorities and options such as the direct hire authority or coordinated interagency recruitment efforts.

We are looking at all available personnel authorities that are currently available. For example, on March 17, the Office of Personnel Management (OPM) authorized the Government-wide use of excepted service appointments (or "Schedule A" Hiring Authority) so agencies can quickly hire additional staff without sacrificing veterans' preferences. On a temporary basis of up to one year, agencies may use this authority to fill positions at any grade level in any geographic location to fill positions needed to carry out provisions of the Recovery Act. OPM also hosted an interagency forum last week, which provided participants with tools for recruitment and hiring.

The Administration has also reviewed a bill introduced on March 18 by Senator Collins and co-sponsored by Senators Kohl and Voinovich, which would authorize Federal agencies to reemploy retired Federal employees on a limited basis without offsetting the annuity from salary. The Administration generally agrees that employing retirees could be a promising means of building capacity within agencies for Recovery Act implementation and generally supports the kinds of additional flexibilities proposed by Senators Collins, Kohl, and Voinovich. I look forward to working with the leadership of OPM to fully engage with Congress on these and other hiring and human capital issues.

**Relating to the issue of human capital, I will briefly speak to some recent developments regarding the structure of Recovery Act leadership and oversight.**

Just two weeks ago, the Administration brought on board Ed DeSeve in a senior role supporting implementation of the Recovery Act. Ed previously served at OMB as Comptroller from 1994-1997, and then as Deputy Director for Management through 1999. He has most recently worked as Chairman of Strategies and Solutions LLP, and at the University of Pennsylvania's Fels Institute of Government. Ed will focus on interagency coordination and lead White House efforts to make sure that the Recovery Act is implemented quickly and effectively. His efforts within the White House work in parallel to, and will be closely coordinated with, the oversight work led by the independent Accountability and Transparency Board, chaired by Earl Devaney.

With these parallel and coordinated leadership structures, the Board and the Administration Recovery team are collectively responsible for shepherding the Recovery Act through successful implementation. Recovery.gov is at the nexus of this collaboration, as the Board has assumed full oversight of the site's content, while OMB will continue to oversee the collection of the underlying data, to be made available for posting at the Board's discretion.

This setup is intended to ensure that the site remains an objective, data-driven resource that can create transparency and accountability, and facilitate the kind of evidence-based decision making that we need for the success of the Recovery Act to continue.

**With that, I'll conclude by reiterating that all levels and branches of government have been entrusted with a great responsibility of helping to lead this nation out of an economic crisis.**

We share the burden of living up to the expectations of the American people, and delivering the transparency, accountability, and performance that we promised.

Thank you, and I look forward to your questions.

TESTIMONY OF THE HONORABLE EARL E. DEVANEY  
CHAIRMAN, RECOVERY ACCOUNTABILITY AND TRANSPARENCY BOARD  
BEFORE THE UNITED STATES SENATE COMMITTEE  
ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
APRIL 2, 2009

Mr. Chairman and members of the Committee, I want to thank you for the opportunity to testify today. I have had the honor of testifying before this Committee in the past as the Inspector General of the Department of the Interior. As you all know, the President has recently appointed me to chair the Recovery Accountability and Transparency Board (the Board), and it is in that capacity that I appear before you today. My testimony will address the current status and mission of the Board, and after I make my opening remarks, I will be glad to answer any questions you have for me.

I am pleased to tell you that the Board has recently obtained office space and continues to acquire a staff of highly skilled oversight and IT professionals. Our first Board meeting was held last week, and we have set in motion a number of initiatives to ensure that the Board fulfills all of its responsibilities under the American Recovery and Reinvestment Act of 2009 (the Recovery Act or Act).

The Members of the Board and I view the Board as having a dual mission. First, the Board is responsible for establishing and maintaining a website, the purpose of which is not only to foster historic levels of transparency of Recovery funds but to do so in a user-friendly manner. Second, the Board will coordinate and conduct oversight of Recovery funds to prevent fraud, waste or abuse.

Even before the Recovery Act was signed into law by the President, the Office of Management and Budget (OMB) and the General Services Administration (GSA) had begun designing the architecture and creating the implementation plan for the website. A great deal of credit must be extended to OMB and GSA for their efforts to launch this website. Because of their efforts, all Americans can visit the website today at Recovery.gov. However, I think it is important to point out that the creation of this website is an evolving process with multiple phases. It is not a single event.

As you know, the Recovery Act vests the Board with the authority to maintain this website. Now that the first phase of getting Recovery.gov up and running has ended, I am eager for the Board to start the second phase of development: The Board will begin to manage the website's design and content, OMB will retain responsibility for the reporting guidance and the collection and verification of data, and GSA will continue to host the website. I am confident that this division of labor will provide the best opportunity to maximize Recovery.gov's use as a transparency and accountability tool, and I am equally confident that we will also have the opportunity to achieve an unprecedented level of citizen participation.

The Board is in the process of obtaining an outside source to conduct an Independent Verification and Validation – referred to as an IV&V – to assess the current state of Recovery.gov. We have also tentatively decided to hold an electronic town hall where the Board and OMB will be able to solicit advice and ideas from the public on new technologies that can help us collect and array data regarding Recovery funds in an innovative way. Soon after this public event, we will conduct a competitive process to select a vendor or vendors to help us build the type of historic website envisioned under the Recovery Act.

Mr. Chairman, I believe James Madison was correct when he said, “A popular government without proper information, or the means of acquiring it, is but a prologue to a farce or a tragedy; or, perhaps, both.” The words of Madison lead me to conclude that the information on Recovery.gov must be easily retrievable and understood by taxpayers, lawmakers and watchdog groups alike and that citizens must be given the opportunity to provide feedback to their government. Indeed, I am excited about the prospect of heightened citizen participation being a force multiplier for Inspectors General (IGs) along with the likely benefit of it helping to drive self-correcting behavior.

Regarding the other half of the Board’s dual mission – accountability – there is also recent news. IGs across the federal government have developed multiple strategies to help prevent fraud, waste or abuse of Recovery funds. In fact, the Committee recently heard testimony about some of these preventive strategies from the Chair of the Council of the Inspectors General on Integrity and Efficiency, Phyllis Fong. While it is not my intention to repeat them all again today, I can tell you that the IGs are quickly transforming those strategies into real action. For example, at least six IGs have already conducted reviews of previously unimplemented IG or Government Accountability Office (GAO) recommendations. These reviews will allow their departments to take corrective actions to ensure that effective controls are in place for handling Recovery funds.

The Department of the Interior Office of Inspector General has developed a risk-based model to use in conjunction with Recovery funds going into grants and is now assisting that Department to develop its own risk model for grants, with the hope of extending the model to contracts and cooperative agreements. The Department of Energy Office of Inspector General has completed 30 fraud awareness briefings nationwide involving more than 2,000 attendees. Several other IGs have audits and evaluations that are about to be released which will include recommendations that will be particularly helpful to their departments for Recovery Act activities.

At our first Board meeting last week, both Phyllis Fong and I supported the Board’s decision to form a new Recovery Funds Working Group which will be co-chaired by Board Member Calvin Scovel, the IG at the Department of Transportation, and a member of the Board’s staff, former IG John Higgins. The purpose of this Working Group will be to ensure the maximum level of coordination and cooperation among IGs necessary to prevent fraud, waste and abuse.



Mr. Chairman, you and the Members of the Committee may have noticed that I have been using the word “prevent” to help describe the Board’s mission of accountability. That is very deliberate on my part.

Most IGs, including myself, generally spend considerable time detecting fraud or waste and then examining such fraudulent or wasteful activities through either a traditional audit or criminal investigation. It strikes me that, although those traditional tools will undoubtedly serve an essential purpose once Recovery funds have been awarded and as they are being spent, IGs may be better able to maximize their value to the accountability goal of the Recovery Act by first concentrating their efforts on prevention. The language of the Recovery Act strongly suggests that IGs and other oversight entities are being asked to minimize the risks inherent in distributing such an extraordinary amount of money and to maximize the opportunities to prevent waste or fraud in the first instance, before it happens.

I foresee the Board actively detecting fraud trends, identifying best practices for conducting reviews, and designing risk-based strategies to help focus the oversight community’s limited resources. The new Recovery Funds Working Group will also serve as a catalyst for an unprecedented leveraging of resources. We will also work closely with the Department of Justice to ensure that when fraud is detected, a swift, coordinated process will follow.

In addition, I can assure each of you that the Board will strive to be as helpful as possible to state and local governments. To that end, the Board’s staff will include audit, investigative, procurement and intergovernmental professionals who, as a key part of their job descriptions, will be responsible for fostering a close working relationship with all of our oversight partners. Clearly, for the Board to accomplish its mission of accountability, we will need to ensure open communications and frequent interactions with state and local auditors, as well as with the GAO.

Finally, I would like to present some of the impending challenges that I see as having the most impact upon the Board and its missions of transparency and accountability. First and foremost is the matter of data quality. Simply stated, the federal government’s systems have never been fully successful at producing timely and reliable data. Add to that problem the difficulty of transmitting and reporting data up through multiple layers of government, as the Recovery Act contemplates, and you begin to understand the basis for my concern.

Second to data quality is the lack of an adequate number of procurement professionals at all levels of government. Federal agencies, in particular, will have great difficulty attracting and hiring enough procurement professionals to minimize the risks associated with moving this amount of money quickly to accomplish the Act’s goals. As you may know, the Act calls for the Board to review whether or not there are sufficient qualified acquisition and grant personnel overseeing Recovery funds and whether they have received adequate training. My staff has already begun the process of doing this review, and I was particularly encouraged by the news that the Office of Personnel

Management has tentative plans to hold a multi-agency job fair to help agencies with their human resource needs in this arena.

Finally, I am concerned there may be a naïve impression that, given the amount of transparency and accountability called for by this Act, little to no fraud or waste will occur. I am afraid that my 38 years of federal enforcement experience informs me that some level of waste or fraud is, regrettably, inevitable. Obviously, the challenge for those of us charged with oversight will be to significantly minimize any such loss. My promise to this Committee today is that my staff, the members of the Board, and I will work tirelessly to reduce those losses to the lowest level possible.

Mr. Chairman and members of the Committee, that concludes my prepared testimony. Thank you for this opportunity. I will be glad to answer any questions you might have.

**Post-Hearing Questions for the Record  
Submitted to the Honorable Robert L. Nabors II  
From Senator Joseph I. Lieberman**

**“Recovery and Reinvestment Spending: Implementing a Bold Oversight Strategy”  
April 2, 2009**

1. *The Federal Financial Assistance Management Improvement Act of 1999 (FFAMIA) required the Director of the Office of Management and Budget to create a common system where those seeking federal grants could apply electronically for those grants and report on the use of the grants received; earlier this year, the Senate passed S. 303, which would extend and expand the requirements of the original FFAMIA. In response to FFAMIA, the federal government established the grants.gov website, but unfortunately, grant recipients still cannot use the website to report on the use of federal grant funds. OMB recently reported problems with grants.gov that were exacerbated under the pressure of a stimulus-related increase in grant applications; as a result, OMB issued a memo on April 8, 2009 requesting more funding from grant-making agencies in order to address immediate needs and make short-term improvements.*

*While short-term improvements to grants.gov are necessary to maintain functionality, larger questions remain for both the maintenance and expansion of grants.gov. The ARRA establishes new reporting requirements for non-federal entities receiving funding through the Act, and we heard testimony that a website (federalreporting.gov) will provide a means for that reporting to be done, and recovery.gov will allow that information to be made publicly available, online. As the recovery.gov website is being built, what steps does OMB intend to take to ensure that the capabilities being built to enable reporting on the spending of stimulus funds will ultimately also be able to be used as the basis for reporting on all federal grant funds – the goal of the original FFAMIA?*

**Response:** OMB is working intensively to provide federal grant recipient reporting information on recovery.gov. OMB is also working closely with the recipient community (e.g., state and local governments) to better understand the challenges of recipient reporting, and in turn, to develop solutions. Once the reporting capabilities are in place for the stimulus funds, OMB intends to broaden these requirements to all Federal funding, including Federal grant awards, to comply with the Federal Funding Accountability and Transparency Act of 2006 (Transparency Act). Indeed, our work with Recovery.gov will provide the first major source of Transparency Act recipient data for USASpending.gov. Our current efforts will also provide lessons learned that will enable OMB to move forward and fully implement the Transparency Act and achieve the goal of the original FFAMIA. We will continue to work closely with the Recovery Board, Federal agencies, and the recipient community to achieve our mutual goals.

**From Senator George V. Voinovich**

1. *On March 9, Director Orszag issued a Memorandum for the Heads of Departments and Agencies regarding "Recovery Act Implementation – Improving Grants.gov and Other Critical Systems" that discussed risks to Grants.gov that are associated with the American Recovery and Reinvestment Act of 2009. I understand that one of the ways OMB plans to address those risks is by allowing some departments and agencies to use means other than Grants.gov to accept grant applications. This solution gravely concerns me because I sponsored the Federal Financial Assistance Management Improvement Act of 1999 (PL 106-107) to simplify grant application and reporting requirements, which led to the creation of Grants.gov, so I strongly believe the federal government should maintain a single website for applicants to electronically apply for federal grants. When the Office of Management and Budget (OMB) makes a decision on what departments and agencies will be allowed to use means other than Grants.gov to accept grant applications, will you provide me with a comprehensive list of those departments and agencies and a description of what means those departments and agencies will use to accept grant applications?*

**Response:** OMB shares your concern and remains committed to the goals of PL 106-107 to create and maintain a single government-wide portal for all grant applicants. Earlier this year, we were concerned that grants.gov would not be able to adequately serve the high volume of activity that was expected, and thus took precautionary measures to avert the degradation of service. This was a difficult decision, but we are committed to improving the capacity of Grants.gov so that it will once again be able to handle all major Federal grant-making agencies.

For the interim, agencies are encouraging programs with viable electronic alternatives to Grants.gov to use them. The following agencies will be accepting some or all applications outside of Grants.gov: Corporation for National and Community Service (CNCS), Department of Defense (DOD), Department of Education (DOED), Department of Energy (DOE), Department of Housing and Urban Development (HUD), Department of Justice (DOJ), Department of Treasury, Department of Transportation (DOT), Environmental Protection Agency (EPA), National Air and Space Administration (NASA), the Department of Homeland Security (DHS), and the National Science Foundation (NSF). You can track the list of agencies planning alternative submission methods at: <http://grants.gov/applicants/bulletin.jsp>.

Let me stress that the temporary use of alternative platforms does not change users' fundamental ability to find and access relevant documents through grants.gov. To the contrary, we are carefully linking all relevant websites in order to minimize the effect of this temporary measure on users' experiences.

2. *At that time, will you also provide me with OMB's guidance to those departments and agencies that makes clear to those departments and agencies that allowing them to use means other than Grants.gov to accept grant applications is a temporary solution for extenuating circumstances, and that all departments and agencies will be expected to again accept grant applications through Grants.gov when the issues associated with the website have been resolved?*

**Response:** OMB has been clear that the use of alternative platforms is a temporary measure to carry Grants.gov through the period of high volume that is expected on account of the Recovery Act. As we are continuing to monitor and evaluate grant volume and management capability, OMB has not set an official date by which agencies must return to Grants.gov for the “apply” function. Guidance on the temporary nature of this transition period for Grants.gov has been given at joint Grants Executive Board/Grants Policy Committee (GEB/GPC) meetings and through ongoing communication with agencies.

Based on our ongoing dialogue with Federal agencies, we estimate that the peak period of traffic on Grants.gov will last from April through August, with elevated levels of grants activity continuing for a number of months thereafter. We view this peak period as an extenuating circumstance that will require Grants.gov to have greater capacity than at other points before and afterwards. While we hope to complete updates to Grants.gov as soon as possible, we will need some amount of time after the peak period has passed in order to assess the proper capacity that Grants.gov will require on an ongoing basis.

3. *On a related matter, I understand that the Department of Health and Human Services (HHS) will have a plan this year to address the issues associated with Grants.gov and to improve that website. When that plan is developed, will you provide me with a copy of that plan and its associated cost estimates?*

**Response:** We will share more detailed plans as they become available. HHS estimates that it will take approximately 60 days from the completion of the acquisition process for the enhancement installation to be finished and in production and that spending for this performance “boost” to be approximately \$5.3 million. HHS has established the following high-level milestones for the planned work:

- Acquisition Completion Date (ACD) + 7 Days: Complete Kick Off Meeting with contractor, project management plan, and order Billed Order of Materials (BOM)
- ACD + 25 Days: Receive Hardware/Software
- ACD + 45 Days: Hardware/Software Installation and Network Configurations Complete
- ACD + 50 Days: Solution Testing, Communicate with Grants.gov Stakeholders, transition to production

- ACD+ 60 Days: Enhancement installation complete and in production.

OMB and HHS are also in the process of improving the governance and oversight structure for Grants.gov.

4. *In his responses to questions for the record following his confirmation hearing, Director Orszag committed to work with the Chairman and I on our legislation, the Federal Financial Assistance Management Improvement Act of 2009 (S. 303), to further improve and streamline the federal grant process. Director Orszag stated, "[t]he reauthorization of the Federal Financial Assistance Management Improvement Act of 1999 would complement [the Federal Funding Accountability and Transparency Act] by enabling us to achieve, along with transparency enhancements, process improvements that lower costs and reduce burden on government agencies and Federal funding recipients." Does OMB remain committed to working with us on this matter and will OMB work with us this year to make any changes to that legislation that are necessary as a result of HHS' plans for Grants.gov?*

**Response:** OMB remains committed to working with Congress to identify and implement legislative changes needed to establish a clear path forward for Grants.gov and to promote economy, efficiency, and effectiveness of the Federal grant-making process.



**United States Senate**  
**Committee on Homeland Security and Governmental Affairs**  
 Chairman Joseph I. Lieberman, ID-Conn.

Opening Statement of Chairman Joseph Lieberman  
 "The American Recovery and Reinvestment Act: Making the Economic Stimulus Work for Connecticut."  
 April 7, 2009  
 Washington, DC

This hearing of the United States Senate Committee on Homeland Security and Governmental Affairs will now come to order. Let me thank all of you for being here.

Let me also thank Eric Bernstein, principal of the Hartford Academy of the Arts for hosting this field hearing and Jim Keller, managing director of the Theatre of the Performing Arts for handling the logistical arrangements. And let me give a particular welcome to the students and teachers of the Greater Hartford Academy of the Arts and the Greater Hartford Academy of Math and Science.

Let me also welcome everyone else who has come, including some in State and local service who are here to join with us in what is a continuing series of hearings that our committee is holding. The first two occurred in Washington. This is the third one, a field hearing, and the basic goal we have is to monitor how the billions of taxpayer dollars that the President requested and Congress approved for the so-called stimulus program are being spent.

Shortly after I was elected to the Senate in 1988, I was down in Washington for some orientation meetings for the new Senators and I was at a reception and John Glenn, who was then the Senator from Ohio—and of course world-famous for being an astronaut—came over to me and he said, "Joe, I'm going to try to return a favor to you that was once done to me."

He said, "Just after I was elected, I was at a reception somewhat like this with the then-Senator from Connecticut, Abraham A. Ribicoff"—probably the students don't remember him, which should inspire some humility in people like me, but others will remember our former governor and Senator from Connecticut. Senator Glenn said, "Ribicoff came over to me and he said 'John, you're going to have the opportunity to select what committees to be on. A lot of times people don't think about the Governmental Affairs Committee, but it's an extraordinary committee. It has the responsibility, among other things, to oversee the expenditure of federal money and to monitor what every department of the federal government is doing and to hold investigations, which over the history of the committee it has done.'" These investigations go back to Senator Harry S Truman, when he investigated, during the Second World War, the spending of money during wartime. There were other hearings held by the committee. Probably the most famous, when I was a kid, was done by the Senator from Tennessee, Estes Kefauver, into organized crime and it goes on and on.

Senator Glenn said, "Why don't you put your name down for it? I don't think there's much interest." Senator Glenn by that time had become Chairman of the Committee. And he said, "I always looks back and I'm grateful to Abe Ribicoff for giving me that suggestion." So I did put it down. It wasn't my first choice, my first choice was the environment committee, which I was lucky enough to get on, but there wasn't much interest in this committee and so I also got put on it.

The students have probably heard about the seniority rule in the Senate. This is the rule that basically says that you get the opportunity to move up in almost all cases based on how long you've been there. Actually, I remember that at the orientation session we had when we first arrived, there was a Senator named Wendell Ford from Kentucky who'd been a Senator for a long time, he came in and said to the ten or eleven of us who were new Senators, "You know, a lot of the things that you're going to find around here, you're not going to

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understand or they actually are going to annoy you.” He said, “That’s the way I felt about the seniority rule when I got here, but you know, the longer I’ve been here, the more sense it makes.”

You never know how your seniority is going to play out because you never know what’s going to happen to the people ahead of you in seniority on the committee. I’ve been very fortunate to become the chairman of this committee.

In 2002-2003, this committee generated the legislation that created the Department of Homeland Security. And when it came time to decide which committee would oversee this new department, they asked us to do that, in part because our committee has had a real reputation for bipartisan work. So the Committee is now known as the Senate Committee on Homeland Security and Governmental Affairs. And I’ve had the privilege to work with two Republican chairs or ranking Republicans when Democrats have been in the majority, Fred Thompson, who left me to go back to “Law and Order” and Susan Collins from Maine.

In a way, I want to use our state as a microcosm of the challenges facing all of our State and local governments as we try to get federal stimulus money moving through our economy, protect and create jobs and make investments in our future. I’m not going to spend much time talking about the economic problems that brought forth the stimulus because we live with them. Last year, American households lost \$11 trillion dollars in value—assets, wealth from the loss of value in our homes and the loss of value in our stock markets in the loss of investments and savings that we have had.

In the State of Connecticut, since the recession began in December ’07, January ’08, we have lost over 50,000 jobs. We had the worst month of job loss in Connecticut in over 15 years in February, when we lost over 15,000 jobs. It is that set of facts that led President Obama and his administration to reach out to Congress and to propose what we call the federal stimulus package; the formal name of it is the *American Recovery and Reinvestment Act*. It is the largest federal appropriation of its kind in American history.

This is not the Great Depression. Unemployment and the loss in the economy are nowhere near as great as it was then and there are the beginnings of some sort of hopefulness. The markets, which measure all this, had their best month in years in March. It was the beginning of economic activity. Consumer spending went up a little bit. The newspapers today here in the State say the Connecticut Business Industry Association did a survey of small businesses in the State and found that they were finding it easier in the month of March to get loans from banks, which had been a real problem.

But State and local governments are hurting and will continue to hurt and until we begin to create jobs again and stop the bleeding off of jobs and people becoming unemployed, we’re not going to be anywhere near where we want to be. That’s what the stimulus package, \$787 billion, authorized over two years, was intended to address. There was a real problem in our economy. Subprime mortgages, loss of housing values, trouble in the financial sector, people unable to borrow money, the beginning of unemployment—real problems.

Those real problems did two things. First, they created understandable anxiety, a lack of confidence in the American people about their futures economically, whether they were going to lose their jobs, or if they had lost wealth in the stock market or their housing values. And so people stopped spending. And spending drives about 70 percent of economic growth in our country. A lot of economists told President Obama and told members of Congress that there was a trillion dollar gap between what the American people would normally spend, what businesses would invest for this year, because businesses would stop investing when they couldn’t borrow the money. And the only entity that could begin to spend and turn the economy around and increase people’s confidence was and is the federal government. That’s why the president made the recommendation to enact a stimulus and why Congress adopted it. I was privileged to be in the middle of the negotiations to not only form the bill, but to get the 60 votes we needed to get it out of the Senate and into a conference committee to pass and be signed by President Obama.

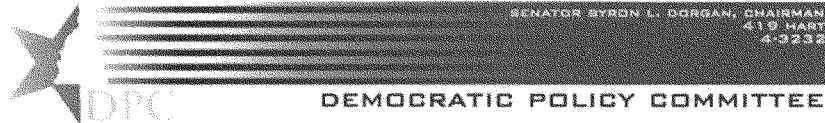
I believe the stimulus package has begun to put money out into the economy in a way that’s working. I think that’s part of why confidence has gone up and why so many economic indicators have gone up. But there’s



a lot more that we've got to do and that's why we're really here this morning. And I will tell you that I think there were two goals the Administration had, and that I think most members of Congress had, for the stimulus. The first was to get money out into the economy to protect and create jobs. The second was to try and do it in a way that would make significant investments in the future for the American people. In other words, not only to stop the bleeding and build up the economy again, but to do it in a way that would be an investment in a better quality of life and sustained economic growth in three particular areas: education, health care and energy independence.

And the State of Connecticut, as I'm sure you've probably heard, under this program, will receive \$2.9 billion in funding. And I'm very glad we've been able to do that. Under the stimulus proposal, the payroll tax reductions that are beginning this month and will reduce the payroll tax for 1.4 million workers in Connecticut and their families; \$400 for a single worker and \$800 for a couple. Some people say that's not a lot of money. For a lot of people in our State right now that's a lot of money. It's going to enable them to maybe pay some bills off, maybe to buy some things that they need that they otherwise wouldn't be able to buy.

So today we are focusing on that \$2.9 billion that's coming to the State of Connecticut for spending and also for redistribution to other entities. And we're privileged to have with us a perfect group of witnesses, one representing the State, the others representing an education group, a health care group and a broader group that speaks for children and the need for social services in our state. So let me go with that to introduction of our witnesses.



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## **The American Recovery and Reinvestment Act of 2009** *Creating Jobs, Investing in Our Country's Future, and Cutting Taxes For the People of Connecticut*

*Today does not mark the end of our economic troubles. Nor does it constitute all of what we must do to turn our economy around. But it does mark the beginning of the end - the beginning of what we need to do to create jobs for Americans scrambling in the wake of layoffs; to provide relief for families worried they won't be able to pay next month's bills; and to set our economy on a firmer foundation, paving the way to long-term growth and prosperity.*

*-President Barack Obama, 2/17/09, Denver, CO*

On February 17, 2009, President Obama signed the *American Recovery and Reinvestment Act of 2009* into law. This urgently-needed legislation requested by President Obama was passed by a 60-vote supermajority in the Senate on February 13. It will create and protect 3.5 million jobs for American workers and begin to put the nation's economy back on track. We are confronting the most severe economic problems in generations as millions of Americans are struggling. That's why the *American Recovery and Reinvestment Act of 2009* will **create good-paying jobs; make investments in America's future; and cut taxes** for working families. Our plan also delivers transparency and accountability to guarantee that all taxpayer money is invested responsibly.

### **What does this mean for Connecticut?**

#### **Job-Creating Investments**

Since the recession began in December 2007, the nation has lost more than 3.6 million jobs, with 50 percent of those losses occurring within the last three months, and the national unemployment rate has skyrocketed to 7.6 percent. Without swift action, economists estimate that an additional five million job losses could occur this year and the unemployment rate could rise to 10 percent.

The *American Recovery and Reinvestment Act of 2009* will create or save 3.5 million good-paying jobs nationally over the next two years, more than 90 percent of which will be in the private sector. According to the White House, **41,000 of these jobs will be in Connecticut**. Getting America back to work is the first step on the road to economic recovery and long-term competitiveness and prosperity.

**Infrastructure and science.** In order to rebuild our weakening economy, these investments in our physical and cyber infrastructure will put Connecticut's immediately to work rebuilding our crumbling roads and bridges, and will also enable the creation of a stronger and more efficient infrastructure for the 21st century economy. According to the Senate Committee on Appropriations, our economic recovery package includes the following estimated benefits for Connecticut:\*

- \$19.7 million through the **Drinking Water State Revolving Fund** to address the backlog of drinking water infrastructure needs
- \$48.8 million through the **Clean Water State Revolving Fund** to address the backlog of clean water infrastructure needs
- \$302.1 million in **Highway Funding** to be used on activities eligible under the Federal-aid Highway Program's Surface Transportation Program and could also include rail and port infrastructure activities at the discretion of the states
- \$137.5 million in **Transit Formula Funding** for investments in mass transit
- \$35.9 million through the **Public Housing Capital Fund** to enable local public housing agencies to address a national \$32 billion backlog in capital needs – especially those improving energy efficiency in aging developments – in this critical element of the nation's affordable housing infrastructure
- \$26.3 million in **HOME Funding** to enable state and local government, in partnership with community-based organizations, to acquire, construct, and rehabilitate affordable housing and provide rental assistance to poor families
- \$17 million through the **Homelessness Prevention Fund** to be used for prevention activities, which include: short or medium-term rental assistance, first and last month's rental payment, or utility payments. As such, most of this funding will go directly into the economy of local communities, as the funds will be used to pay housing and other associated costs in the private market

**Education and Training in Connecticut.** In order to compete in the 21st Century, we must have a well-educated workforce, capable of adapting to an ever-changing economic environment. Investing in education now will ensure that the next generation of Connecticut's workers is ready and able to meet the challenge of global competition. In the near-term, millions of workers have seen their jobs disappear, and find themselves unable to match their skill sets with existing opportunities. Providing job training in new and expanding fields will help to lower the unemployment rate and help today's workers better compete against foreign competition.

The Congressional Research Service estimates that our economic plan includes \$545.8 million through the **State Fiscal Stabilization Funds** to local school districts and public colleges and universities in Connecticut and additional funding for other high-priority needs such as public safety and other critical services, which may include education

According to the Senate Committee on Appropriations, our economic recovery package includes the following estimated benefits for Connecticut:\*

- \$133 million for **Special Education Part B State Grants** to help improve educational outcomes for individuals with disabilities, raising the federal contribution to nearly 40 percent, the level established when the law was authorized more than 30 years ago

- \$4.8 million in **education technology** funds to purchase up-to-date computers and software and provide professional development to ensure the technology is used effectively in the classroom
- \$97.1 million for **Title I Education for the Disadvantaged** to help close the achievement gap and enable disadvantaged students to reach their potential
- \$4.4 million in **State Employment Service Grants** to match unemployed individuals to job openings through state employment service agencies and allow Connecticut to provide customized reemployment services
- \$13.5 million in **Dislocated Workers State Grants**, particularly for grants that support immediate strategies for regions and communities to meet their need for skilled workers, as well as longer-term plans to build targeted industry clusters with better training and a more productive workforce
- \$4.4 million for Department of Labor's **Adult State Grants**
- \$11.1 million for Department of Labor's **Youth State Grants**
- \$3.5 million for **Vocational Rehabilitation** to help individuals with disabilities prepare for and sustain gainful employment

According to the White House, the economic recovery package also includes more Pell Grants for the **52,000 Pell Grant recipients** in Connecticut.

**Connecticut's Energy.** The *American Recovery and Reinvestment Act of 2009* provides investments in areas critical to the development of clean, efficient, American energy, including modernizing energy transmission, research and development of renewable energy technologies, and modernizing and upgrading government buildings and vehicles. According to the Senate Committee on Appropriations, our economic recovery package includes the following estimated benefits for Connecticut:\*

- \$39.1 million through the **State Energy Program**
- \$65.8 million through the **Weatherization Assistance Program**

**Protecting the Vulnerable in Connecticut.** The current economic crisis has affected all Connecticut residents, but none more so than the most vulnerable among us. The spending proposed here will serve to lessen the blow of the current recession, providing immediate relief for children, the poor, and others who may find themselves struggling to put food on the table or a roof over their head. It will also address the urgent need to provide safe and secure places to live, even in neighborhoods that are struggling with high unemployment and surging foreclosure rates. According to the Senate Committee on Appropriations, our economic recovery package includes the following estimated benefits in the state:\*

- \$922,028 for **National School Lunch Program Equipment Assistance**
- \$887,393 through the **Emergency Food Assistance Program**
- \$169.2 million in **Supplemental Nutrition Assistance Program** benefits (formerly Food Stamps)
- \$1.1 million for the **Emergency Food and Shelter Program**, which provides grants to nonprofit and faith-based organizations at the local level to supplement their programs for emergency food and shelter to provide for the immediate needs of the homeless
- \$13.7 million in **Child Care and Development Block Grants** to provide quality child care services for in low-income families who increasingly are unable to afford the high cost of day care

- \$5 million for **Head Start** to allow additional children to participate in this program, which provides development, educational, health, nutritional, social and other activities that prepare children to succeed in school
- \$12.1 million in **Community Services Block Grants** to local community action agencies for services to the growing numbers of low-income families hurt by the economic crisis, such as housing and mortgage counseling, jobs skills training, food pantry assistance, as well as benefits outreach and enrollment
- \$766,530 for **Senior Meals Programs** to help senior meals programs cope with steep increases in food and fuel costs. Many programs are reducing meal deliveries to seniors or closing meal sites

According to the Center for Law and Social Policy, Connecticut will receive an estimated \$17 million, benefiting an estimated **2,600 households** in Connecticut for **Homelessness Prevention activities**, which include short- to medium-term rental assistance, housing relocation and stabilization assistance, and rapid re-housing assistance for those who have become homeless

**Law Enforcement in Connecticut.** Nearly every sector of the American job market has suffered job loss and programming cuts, including state and local law enforcement. Cuts in this field can have a devastating direct and indirect effect on the health of a community by way of increased crime, lowered property values, business closings, and the loss of good paying, upwardly-mobile, middle class growing jobs. According to the Senate Committee on Appropriations, our economic recovery package includes the following estimated benefits for Connecticut:\*

- \$21.1 million in **Byrne/JAG grants** to support law enforcement efforts
- \$ 783,714 for **crime victims compensation and assistance**
- \$1 million in **Internet Crimes Against Children Grants** to help law enforcement agencies enhance their investigative response to offenders who use the Internet, online communication systems, or other computer technology to sexually exploit children
- \$2.2 million in **Violence Against Women Grants** for victim services programs to improve the criminal justice system's response to violent crimes against women and to assist victims of domestic violence, dating violence, sexual assault and stalking who are in need of transitional housing, short-term housing assistance, and related support services

The Center for Law and Social Policy estimates that the *American Recovery and Reinvestment Act of 2009* also includes \$16.1 million for Connecticut in federal matching funds for child support enforcement, which will improve Connecticut's ability to collect child support – a critical safety net for struggling families and a reliable source of economic stimulus because those families reinvest the money into the local economy for basic needs.

#### **Extended Unemployment Insurance for Connecticut**

Unemployment in Connecticut stood at 7.1 percent in December 2008 (the last month for which we have data). The Department of Labor estimates that Connecticut could receive \$88.4 million in new funding if Connecticut fully enacts the UI modernization incentives that the new law provides.

According to the National Employment Law Project, this means that an additional \$100 in unemployment insurance benefits will be offered to approximately **278,000 workers** who have lost their jobs in this recession.

#### **Fiscal Relief for Connecticut Through FMAP**

Rising unemployment rates mean that more people are losing their health insurance and relying on Medicaid to maintain coverage. The *American Recovery and Reinvestment Act of 2009* provides almost \$87 billion over the next two years in additional federal matching funds to help states, like Connecticut, maintain their Medicaid programs. Already 28 states have proposed or enacted cuts to public health programs and state budget deficits continue to grow. This temporary, targeted funding is critical to ensuring that states experiencing significant unemployment receive additional funding. Connecticut will receive \$1.32 billion that will help Connecticut avoid cutting eligibility for Medicaid and maintain the services available to recipients.

#### **Tax Relief for Connecticut Families and Businesses**

According to the Senate Committee on Finance, the following are examples of tax provisions in the *American Recovery and Reinvestment Act of 2009* that will help Connecticut businesses and families, create jobs and get Connecticut's economy moving:

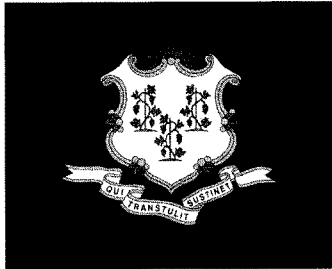
- Up to \$400 for workers (or \$800 for married couples) in the new **Making Work Pay Tax Credit for 1.4 million workers** and their families in Connecticut
- \$250 to Social Security beneficiaries, SSI recipients, and disabled veterans
- \$2,500 for **30,000 additional families** in Connecticut that will qualify for the new **American Opportunity Tax Credit** that makes college more affordable for 3.8 million families nationwide
- **Extended and increased first-time Homebuyer Tax Credit** to both help aspiring homeowners and stabilize plummeting home prices
- **Extended Bonus Depreciation and Small Business Expensing** through 2009, allowing businesses that make capital investments to immediately deduct one-half the cost. Small businesses can immediately deduct 100 percent of the cost of these investments

The *American Recovery and Reinvestment Act of 2009* would protect over 26 million working families across the nation from the **Alternative Minimum Tax**, representing thousands of dollars in additional income taxes. According to the Congressional Research Service, 617,000 Connecticut residents would be protected from the Alternative Minimum Tax in 2009.

***\*Note that this provides estimates of highlights of the Division A of the American Recovery and Reinvestment Act of 2009 as of February 19, 2009. It is not a complete listing of all the benefits for Connecticut in the economic recovery package and some numbers may have been updated by agencies since this list was compiled.***

## **American Reinvestment and Recovery Act of 2009**

Creating Jobs, Investing in Our Country's Future,  
Cutting Taxes for the People of Connecticut



### **Connecticut will receive \$2.9 billion from the stimulus bill**

The following are examples of funds that have been obligated for Connecticut:

- \$1.3 billion in matching funds for Medicaid
- \$765 million for education
- \$137.5 million for transit programs
- \$105 million to replace Niantic River Bridge on Amtrak's Northeast Corridor
- \$100 million for weatherization and other energy projects
- \$48 million for the Clean Water State Revolving Fund program
- \$25 million in guaranteed housing loans
- \$24.5 million for energy projects
- \$20.5 million for first responder and criminal justice programs
- \$8 million for Bradley International Airport runway repairs
- \$4 million for National Guard, Marine Corps Reserve facility
- \$3.7 million for community health centers
- \$3.2 million for courthouse energy efficiency improvements
- \$1.1 million for senior nutrition assistance
- \$350,000 for runway improvements at Danbury Municipal Airport

\* Connecticut's exact share of stimulus funding for other programs has yet to be determined\*



**STATE OF CONNECTICUT**  
**OFFICE OF POLICY AND MANAGEMENT**  
**OFFICE OF THE SECRETARY**

**United States Senate**

Homeland Security and Government Affairs Committee field hearing

Tuesday, April 7, 2009

The American Recovery and Reinvestment Act:  
 Making the Economic Stimulus Work for Connecticut

Remarks of Robert L. Genuario, Secretary, Connecticut Office of Policy and Management

Senator Lieberman and distinguished members of the Homeland Security and Government Affairs Committee, I am Robert Genuario and I am Secretary of the Connecticut Office of Policy and Management. On behalf of Governor Rell, I thank you for the opportunity to speak with you today and for your efforts in bringing the federal economic stimulus package forward for our state and for our country. These are difficult days for those of us charged with serving the public and we appreciate the collaboration and cooperation that we have seen from our partners in the federal government. With patience and perseverance, I am confident that we will emerge a stronger state and nation.

**Introduction**

The American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law by President Obama on February 17th, 2009, and includes measures to modernize our nation's infrastructure, enhance energy independence, expand educational opportunities, preserve and improve affordable health care, provide tax relief, and protect those in greatest need during this extraordinary economic downturn.

In an effort to create job opportunities for Connecticut residents and help the state's communities and businesses prosper, Governor Rell has taken a number of steps to maximize the effectiveness of the ARRA in Connecticut. The Governor has:

- created the Connecticut Recovery Working Group to identify and select projects of the "shovel ready" nature, work that has primarily focused on the transportation aspects of the Act;
- established a process to coordinate the activities of state agencies through regular meetings involving Governor's office staff and core agencies that have the bulk of the formula-based programs to implement - OPM, DOT, DECD, DPH, DSS, Labor, DEP, DPS and Education;



- initiated efforts to share and receive information from municipal leaders on stimulus activities in their communities; and
- formalized procedures and policies for promoting transparency and ensuring accountability, including the establishment of the state's economic recovery website, [www.recovery.ct.gov](http://www.recovery.ct.gov).

#### **Accountability and Transparency**

Concerning accountability and transparency, Governor Rell has issued Executive Order No. 25, which calls for the creation of a State Accountability Officer, a State Transparency Officer and Stimulus Project Oversight Officer.

- The State Accountability Officer will be responsible for ensuring the state provides all reports, certifications and assurances required by the ARRA.
- The Transparency Officer will maintain and keep current the CT Recovery Web site, posting all applications, receipts for spending stimulus funds and other required documentation.
- The Stimulus Project Oversight Officer, will act as the state's "clerk of the works," coordinating with every state agency receiving stimulus funds and will oversee the progress of all stimulus-funded infrastructure projects, ensuring they have the required permits and applications and meet deadlines.

The Executive Order, signed March 23, also requires that every state agency that applies for or receives stimulus funds appoint an agency accountability officer responsible to ensure that the money is used in accordance with the ARRA. Each agency is also required to maintain a detailed Web page on the agency's Web site, listing the agency's stimulus activities.

The federal act also mandates that states make public any contact made with lobbyists and consultants. Governor Rell has said that the State of Connecticut will post a log every Monday on the official CT Recovery Web site listing any contact Executive Branch employees have had with registered lobbyist and consultants concerning projects, issues and other topics related to the ARRA.

#### **Amount and Type of Assistance**

Over the course of three fiscal years, the state is expected to receive more than \$3 billion in formula-based funding through the ARRA. Of this amount, about \$1.3 billion is in Medicaid funds; \$550 million is in the State Stabilization funding, primarily targeted to education and we expect to effectuate that through the state's Education Cost Sharing program and another \$150 million in other education programs such as Special Education and school technology; \$450 million is in transportation infrastructure moneys; \$48.5 million is in Clean Water funding; \$64 million is in Weatherization funds; and \$38.5 will be coming for the State Energy Program.

Considerable funding is also available for unemployment insurance benefits - since March 2<sup>nd</sup>, an extra \$25 has been included in every benefit check - and benefits have been extended through the end of year. \$87 million is available to Connecticut for the Unemployment Insurance Modernization Initiative. We will need to make a modest improvement to our unemployment

benefit structure in order to be eligible for this funding. The Governor has proposed the modification and the legislature is poised to adopt it.

Coupled with this is new funding for workforce training initiatives - Workforce Investment Act (adults and youth), Dislocated Workers, etc., additional funding will be available through competitive opportunities for training in areas considered "emerging or high-growth" such as green collar jobs, health information technology, and in areas where there are shortages - allied health, for example.

#### **Impact on State Budget**

With regard to the state budget, we are in the middle of our legislative session and significant work remains to be done before we reach agreement with the General Assembly on a final budget for the next two years. We have sought and received guidance from the relevant federal authorities as to how the state may utilize stimulus funds in our state budget. That guidance has generally been helpful but a number of significant issues remain to be resolved. We look forward to working on those matters with the relevant federal authorities.

With regard to education funding, the ARRA provides about \$541.9 million in State Fiscal Stabilization Funding (SFSF) for Connecticut. Of this funding, 82% or \$444 million must be used specifically for one of two purposes:

- Restore to the greater of FY 2008 or FY 2009 funding levels for ECS in FY 2009, 2010 or 2011; and
- Restore to the greater of FY 2008 or FY 2009 funding levels for higher education institutions in FY 2009, 2010 or 2011.

It appears that the intent of this part of the stimulus was to provide funding for states to avoid budget cuts that may reduce education efforts. Our budget was formulated with the express intent of using this funding to maintain our education funding levels. Therefore, the Governor's proposed budget does not reduce ECS at all and maintains funding to the higher education institutions at FY 09 levels, after administrative rescissions made necessary by our current year deficit. Given those facts, it is unclear how much funding we may qualify for, however, we may need to modify our budget in order to maximize this education funding. The result will be the same; local boards of education will receive the same amount of funding that they received in fiscal year 2009 pursuant to the ECS formula and other major educational grants. It appears to be a rather curious technical requirement, but one that the state can adjust to.

With regard to the Medicaid funding, we have recognized a need to modify the Governor's budget proposal in light of guidance we have received. There are a couple of items that will likely have to be dropped revision based on CMS's written interpretation: a proposal to impose premiums on Adults in the state's HUSY program (\$8.8 million in FY10, \$9.3 million in FY11) and a proposal to eliminate self-declaration (\$2 million in FY10 & FY11). According to CMS' interpretation, those two proposals are not allowed due to the maintenance of eligibility requirements.

We are aware of some arguments being made by advocates about other Medicaid budget proposals. The enhanced Medicaid reimbursement provided by ARRA is part of the state's anticipated revenue for the FY10-11 biennium, as well as for FY 09. As noted in the Governor's

budget document, “even with the use of the federal stimulus funding, the dedication of the Budget Reserve Fund and aggressive restraint on spending designed to return to core government functions” the state still needs to tap other one-time revenue sources in order to provide additional resources for FY11.

While Medicaid spending increases touted by various advocates may all be for worthwhile programs, given the deterioration of our revenue streams, fiscal restraint is necessary. In short, service and program expansions during this recessionary period are simply not achievable. Moreover, between the exhaustion of the state budget reserve fund by FY '11 and the termination of all stimulus funding, the state will face a structural hole of some significance in its budgetary planning for FY 2012.

In addition, a proposal to transfer some special funds dealing with energy issues will not go forward given our need to maintain efforts in that area in order to receive the stimulus funds for energy efficiency and weatherization.

#### **Conclusion**

In the days and weeks ahead, state agencies will be developing plans in response to funding opportunities associated with the ARRA. The plans will be published both on Connecticut's Recovery website and in the ARRA section of the relevant agency's website.

In addition, there are numerous reporting requirements associated with ARRA funding. Agencies receiving ARRA funding are required to submit periodic and timely reports to the federal agency administering the funding. These reports are to include information as to how the funding is being used and provide information on the number of jobs retained or created. These reports will also be found on our main CT recovery website as well as on individual state agency websites.

Thank you for the opportunity to speak with you today and I will be happy to respond to any questions you may have.



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Affiliated with the  
National Education  
Association

*Testimony of*

**Dr. John Yrchik**  
*Executive Director, Connecticut Education Association*

*Before the*

**United States Senate Committee on Homeland Security and  
Governmental Affairs**

**April 7, 2009**

Good morning Chairman Lieberman and distinguished guests. Thank you for your invitation to submit testimony at this field hearing on *The American Recovery and Reinvestment Act: Making the Economic Stimulus Work for Connecticut.* "

I am Dr. John Yrchik, the Executive Director of the Connecticut Education Association, representing more than 37,000 Connecticut teachers.

I would first like to thank you Senator as well as Senator Dodd and other members of the Connecticut Congressional delegation for your roles in assuring passage of this critical piece of legislation.

The Act's sheer breadth – generating investment in roads, energy, housing, health, small business and job training among other areas – is as promising to short term recovery as it is to the long-term growth and renewal. We commend you and other members of Congress for recognizing the critical role education plays in stimulating our economy and enhancing America's competitiveness in an increasingly complex and interconnected international economy.

The amount of education aid that will flow to Connecticut under the ARRA, excluding competitive grants, is \$772 million, representing an unprecedented infusion of federal money into Connecticut's schools. It is unprecedented in two ways: in size and in nature. This is the first time the federal government has ever provided direct support for state aid to municipalities.

NEA Research has estimated that in the absence of ARRA over 600,000 education jobs in 2009 and over 582,000 education jobs in 2010 may well have been lost due to the current funding gaps in many states.<sup>1</sup> Even with the enormous infusion of federal dollars into education in our state, however, several states – Connecticut included – are expected to see layoffs even after utilizing stimulus funds.<sup>2</sup> As is discussed later in my testimony, we believe that additional clarity and guidance on prioritization, particularly with respect to local spending of IDEA dollars, could prevent significant numbers of projected layoffs in Connecticut.

The economic distress experienced in other states has been exacerbated in Connecticut by the high concentration of financial sector jobs. More than 7.5% of Connecticut's jobs are in the financial services sector, a concentration almost 60% higher than the national average. Our state ranks number one in the concentration of insurance jobs, two in the concentration of securities jobs, and third in funds-and-trusts. Jobs in the financial services sector have much higher multiplier effects on the larger economy than jobs in other sectors, making our state especially vulnerable to crises in the financial sector.<sup>3</sup>

Because of the continuing downward economic spiral, Connecticut's projected budget deficit for the next two years (according to the Office of Fiscal Analysis) is \$8.7 billion. This has placed stress on every area of state and municipal budgets. It is not an exaggeration to say that assistance provided under the ARRA has averted a meltdown of state and local governments that would be at least commensurate with the meltdown of the larger economy.

<sup>1</sup> Current Economic Crisis and K-12 Jobs: A State-by-State Analysis; National Education Association, March 3, 2009.

<sup>2</sup> The other states are California, Delaware, Massachusetts, Nevada, New Jersey, and Rhode Island.

<sup>3</sup> Steven P. Lanza, "Financial Meltdown: How Toxic the Fallout in Connecticut," *The Connecticut Economy* (Winter 2009), p 6.

**The State Fiscal Stabilization Fund**

Connecticut is one of a relatively small number of states that are proposing to use the state fiscal stabilization fund to supplant education aid that the state currently provides to municipalities under its current funding formula. Governors or legislatures in Illinois, Kansas, Michigan, Rhode Island, and Texas are proposing to do the same.<sup>4</sup>

Our state may be alone, however, in using virtually the entirety of the Education Stabilization Fund and the Government Services Fund (that together comprise the State Fiscal Stabilization Fund) to backfill existing state education aid to municipalities with federal dollars. By doing this, the state of Connecticut has effectively reduced its own commitment to basic education grants by 14%.

Connecticut is allowed to use the entirety of the State Fiscal Stabilization Fund to supplant state funds for education because the federal stimulus comes on the heels of an historic increase in state education funding to its 169 school districts. In FY08, the state made great strides by increasing funding to the state's education formula aid to towns (ECS) by 13.42%. Another 4.42% was added for FY 09. These increases represented two steps forward toward the long-held goal of increasing the state's share of local education funding to 50%.<sup>5</sup>

As the Senator is aware, the final Maintenance of Effort provision enacted in the ARRA pegged state education funding baselines at FY06 levels. The 2006 baseline predates Connecticut's earnest movement toward its goal of providing 50% funding to LEAs. The state contributed \$1.619 billion to the Education Cost Sharing formula in 2005-06 and \$1.889 billion today, a difference of \$270 million per year.

In states where FY07 or FY08 increases are not substantially higher than FY06 levels, the addition of stabilization funds to the FY06 baseline can mean increased formula funding for FY09. In Connecticut, however, where substantial increases were enacted in FY07 and FY08, the comparatively low FY06 baseline means that the Governor can choose to reduce the actual expenditure of state dollars by \$540 million over a two year period to

<sup>4</sup> "Michele, McNeill, "State, Local Officials Clash on Use of Stimulus Funds," *Education Week*, April 1, 2009, p. 24.

<sup>5</sup> The state's share of education rose from a low of 38% in FY04 to 43.1% in FY08. If the entire state fiscal stabilization fund is used to supplant state dollars, the state share of education will drop to 39.6% next year.

meet the FY09 levels required by the ARRA.<sup>6</sup> This, in fact, is what our Governor has chosen to do.

Connecticut's governor did have the option of using stabilization funds to exceed the FY09 appropriation. She chose not to do so. By sweeping the \$540 million that had previously been allocated to ECS into other parts of the General Fund and using the ARRA stabilization dollars to backfill (supplant) state funding for ECS, the Governor's proposed budget uses 14% fewer state dollars to fund ECS than would have been necessary if not for the ARRA.

With added mandates and increases in standard operating costs, flat-funding actually represents a cut in funding to LEAs. The Legislature's Office of Fiscal Analysis estimates the funding for FY10 current services would require an increase of about 4% over FY09. Coupled with the Governor's 14% sweep of existing state dollars into other areas of the budget, the difference between what the state has committed to ECS and what would be needed to provide ECS at the level of current services next year is about \$340 million. This means that next year, the state will be contributing 21% less than what it would contribute if it merely provided an increase sufficient to maintain current services at this year's ECS allocation.

CEA recognizes that due to the relatively large ECS increases since 2006 that Connecticut may represent an anomaly. We are pleased with the federal commitment to stabilizing state education funding and we must note that as difficult as the situation is here now, it would undoubtedly be worse had the ARRA not passed Congress. It is my belief that the ARRA has averted an educational crisis in our state.

By way of illustration, in responding to the Governor's request to cut 10% from its budget, the State Department of Education submitted a budget in January that represented a 12% cut in ECS aid. Had a cut of that magnitude or anything close to that passed in this year's budget, the result in school districts across the state would have been catastrophic. The stimulus provided an immediate reprieve from the dire scenarios that were being spun as a result of the State Board's action. Because the reprieve was granted with one time funds, however, it is important for the state to have a plan to replace the

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<sup>6</sup> The entire State Fiscal Stabilization Fund (both components) provides \$542 million over a two-year period.

funds when the stimulus runs out in two years. If it doesn't, we have only postponed a day of reckoning.

An additional challenge needs to be met with respect to the State Fiscal Stabilization Fund. As a condition of receiving the funds, governors are requested to make a commitment to four essential areas of education reform: teacher effectiveness, standards and assessments, improving achievement in low-performing schools, and creating systems that track student progress. Governor Rell needs to show in the final biennial budget adopted by the General Assembly that the state is making progress in these areas.

In the Governor's original budget proposal to the General Assembly, she cut all funding for a new teacher mentor program that was designed to replace an ineffective teacher induction program. This was one of the state's principal areas of commitment to effective teaching and its elimination has to be viewed as significant.

In another move, the Governor cut all funding to a promising new program called CommPACT Schools, an unprecedented collaboration of Connecticut's Neag School of Education at the University of Connecticut and six of the state's leading education organizations. This effort was targeted at improving student achievement in some of Connecticut's lowest performing urban schools. Modeled in part after Boston's successful Pilot Schools, CommPACT schools bring together a school's stakeholders to redefine and reform the educational process at the school site. It is both collaborative and research-based.

Funding for both of these programs has since been restored in the latest budget proposal from the General Assembly. In my reading of the federal government's conditions attached to the stimulus package, it would appear important that these programs remain intact as a condition of the state's receiving its full share of Phase II funding under the State Fiscal Stabilization Program.

Lastly, with respect to transparency, we believe that our SEA's current reporting and audit requirements (referred to as the ED001 report) are comprehensive. However, since the stabilization funds pass to schools via the ECS grant, we also believe that recipients of ECS funds, which are the municipalities, should report the major components of how these funds were allocated. We want to ensure that they are used for the exclusive purpose of education and not to provide tax relief or serve other purposes at the



municipal level. The federal government should be provided with assurance that the stabilization funds were directed to their stated purpose of supporting education and permit the state to monitor whether municipalities have been complying with statutory non-supplant requirements.

### IDEA

While the Governor of Connecticut has shown almost breathtaking willingness to supplant state education dollars with federal dollars, by contrast, local school boards and superintendents have been remarkably inflexible to date in maximizing the use of ARRA funds to prevent layoffs and positions. This has become a serious concern.

The stimulus bill will provide Connecticut an additional \$133 million for IDEA, Part B. Under the latest reauthorization of IDEA, an LEA can use up to 50% of an increase from the previous year to supplant what it is spending on special education from its own share of state and local funds. The funds thus freed up can be used for any ESEA purpose, which means virtually any educational purpose. They certainly can be used for salaries and other personnel-related costs.

However, to date, many Connecticut superintendents have exhibited a reluctance to use a portion of the IDEA increases to reduce layoffs and reductions in education jobs. Some have indicated an interest in purchasing Smart Boards and iPods and making other one-time expenditures. This is permitted under IDEA. While one time-expenditures such as assistive technology can be beneficial, making such expenditures at the expense of jobs runs contrary to the primary goal of the ARRA and compromises the current level of quality of educational services.

Connecticut's State Department of Education (SDE) bears some responsibility for this state of affairs. At a March 17<sup>th</sup> meeting of superintendents on the stimulus, the SDE provided guidance on the use of IDEA funds. It included no mention of the provision of IDEA that would allow 50% of any increase to supplant local special education expenditures.

Under Section 613(a)(2)(C) of IDEA, school districts can reduce their local share of spending on special education by 50% of the increase they receive in federal IDEA funds. This "freed-up" money can be used to prevent layoffs, to hire new employees, or

program improvements and expansions (purposes that meet the broad conditions of federal education funding uses permitted by the “Elementary and Secondary Education Act”).

Only recently has a letter gone out from Connecticut’s Commissioner of Education stating that in fact 50% of any increase in IDEA funds can be used to retain staff. It does not, however, indicate that retaining jobs is the priority of the funds provided in the ARRA and actually discourages districts from using funds to bolster funds available for personnel. While acknowledging the using that freed up funds “will allow districts to address possible budget losses with freed up funds from one’s own special education budget,” the letter goes on to say:

The disadvantage of this strategy, however, is that when the ARRA IDEA funds disappear in two years, one’s local special education budget line item will have been reduced by the amount spent on ESEA activities. This will remain a hole in the budget unless it is made up thereafter by increases to one’s local special education budget.”<sup>7</sup>

In the first place, if a district chooses to use 50% of an IDEA increase to prevent layoffs or retain positions, its maintenance of effort requirement under IDEA is reduced accordingly. While it is true that if the increased funds disappear after two years (a condition that is by no means certain to come to pass), a district will have to replace those funds with local funds in order to keep the positions. At the same time, the need to avoid the immediate deleterious effects associated with a reduction in teaching positions would seem to outweigh any problems associated with uncertainties about how the funds will be replaced. The Governor appears to have made precisely such a calculation with respect to the use of the State Fiscal Stabilization Fund.

As of April 1, a statutory deadline for Boards of Education to issue non-renewals of non-tenured teacher contracts, 1,424 teachers had received layoff notices across Connecticut. More than 600 additional layoffs are threatened in other districts.

The impact is not just an urban or rural phenomenon – teachers in wealthier districts have not been immune. Weston, the state’s 6<sup>th</sup> wealthiest town issued 12 layoff notices. Guilford, which is the state’s 38<sup>th</sup> wealthiest town, issued 68. Cheshire (ranked 62<sup>nd</sup> in

<sup>7</sup> Letter from Commissioner of Education Mark McQuillan to Connecticut superintendents, March 27, 2009.

wealth) issued 85. Bethel (65<sup>th</sup>) initially issued 108, representing 42% of its teaching force, before recalling 58 of them. In all instances of layoffs, the uncertainty such actions brought to teachers' lives is palpable.

The related economic impact of these layoffs is significant. Not only would the Connecticut economy keep an estimated \$59 million in teachers' salaries if these teachers were retained, but according to NEA research restoring the more than 1,424 layoffs would generate over \$33 million in additional personal income beyond that.

We continue to urge Superintendents and Boards of Education to use ARRA funds to save jobs and programs for students. Spending these funds on goods, not people, will smother the effects of the federal stimulus in our communities.

We believe stronger direction from the US DOE and Congress could result in IDEA funds being utilized to offset these layoffs. The cost of restoring one teacher's job is about \$53,914,<sup>8</sup> including roll-up (or overhead) costs.<sup>9</sup> If LEAs are urged to redirect IDEA money equal to 50% of the supplemental funds, as they are permitted to do by law, \$66.5 million could be targeted to preventing layoffs. This alone would save 1,233 of the potential layoffs over two years (over 600 jobs per year).

#### **Title I, Part A**

Connecticut will receive \$97 million in Title I, Part A funding. Of this \$72 million will go directly to school districts and \$25 million will be used for school improvement activities. To put this into perspective, in FY 09 Connecticut received \$102 million in

<sup>8</sup> Layoffs impact teachers across the experience spectrum, but fall disproportionately on newer, younger, and non-tenured teachers. To estimate the average salary cost of a displaced teacher, the average second salary step in Connecticut was chosen as a baseline (\$41,684). The average total cost to the Connecticut districts for health insurance coverage is \$11,517 per teacher. Including workers compensation and Medicare contributions, the total salary cost to a district, including roll-up or overhead is about \$53,914.

<sup>9</sup> Insurance rates for single, family and Plus 1 coverage derived from actual district insurance data collected March 2009 and are inclusive of Rx. Usage weights of .33 (Single) .25 (Plus 1) and .42 (Family) were derived from a sample of 14 districts and applied to generate a weighted average insurance cost of \$13,649 per teacher. This amount, which represents the total cost, was reduced by the average premium cost share paid by the employee of 15.77%. Total cost includes Medicare at 0.0145% of salary and workers compensation costs of roughly \$130 per teacher. Adequate data on the cost of dental plans was not available at this time.

Title I funding from the federal government. The infusion of funds under ARRA almost doubles our current level of funding.

A perennial criticism of No Child Left Behind has been that it was all mandates and no resources. In a law with many problems, the inadequacy of Title I funding was one of the most obvious and severe. With the near doubling of funding in this category and the large amount of funding available for school improvement efforts, it would appear that we are closer to our original goal of properly funding the law.

As noted earlier, however, these are not ordinary times. The failure to maintain ECS at its current services, a reluctance of school administrators to use additional IDEA funds to prevent layoffs, the slashing of municipal budgets, the widespread layoffs of teachers, the elimination of teaching positions, and the elimination and/or reduction of programs provides a grim context for the infusion of new Title I funds.

These resources enter schools precisely when people and programs are vanishing as a result of reduced budgets. If almost \$100 million in new Title I money came into schools when other funding streams were also increasing as was the case in previous years, it would undoubtedly have an enormous positive effect in producing new professional development programs, pre-K opportunities, tutoring, school-based literacy efforts, and other programs that we know improve student achievement.

In the present setting, however, when many core educational programs are being challenged or eliminated, it is difficult to assess whether the additional Title I funding will be able to compensate for the losses elsewhere. The jury is out on this question.

As with IDEA, we need clear guidance on the ability of districts to use the Title I money to supplant existing district funds. Supplanting is more difficult under Title I than IDEA, but U.S. Department of Education Guidance suggests that it is possible. An LEA may generally not use Title I, Part A funds to pay for activities that it would have conducted in the absence of Title I funds. However, it can overcome the presumption that it would have conducted the activity anyway without the funds if it can "demonstrate that there was a reduction in the amount of non-Federal funds available to the LEA to pay for the

activity previously supported by non-Federal funds or the LEA can demonstrate that its educational priorities with respect to its use of non-Federal funds have changed.”<sup>10</sup>

In the area of Title I, there is a need for further clarity from the U.S. Department of Education about the potential use of waivers to supplant Title I funds when appropriate to maintain local education programs. Left to be worked out is whether state departments of education will have the right to grant waivers of Title I’s maintenance of effort requirement and whether districts will have the option of appealing directly to the U.S. Department of Education in the event that waivers are not granted within a state. Also needed is clarity from the U.S. Department of Education on the process for both states and school districts to gain approval from the Secretary to use State Fiscal Stabilization Funds to meet maintenance of effort requirements under Title I and IDEA.

We hold that since the infusion of supplemental funds is anticipated to lapse after 2010, funds associated with IDEA and Title I, Part A these funds can and should be used to bridge the gaps in local budgets for two years with the expectation that revenue streams will show recovery by 2011. We would also strongly urge the President and Congress to continue their support for additional allocations for IDEA and Title I, Part A past 2010 to help states address the continuing unmet needs.

Foremost among our needs at this time, however, is the need for clarity regarding the use of these funds to prevent job losses. It is our hope that with the recent clarification from the US DOE and some sort of expedited process for waivers to be granted for the use of Title I funds, LEAs will target available funds toward preventing job losses and retaining positions.

Finally, we recognize that with such an infusion of taxpayers’ dollars comes the need for ensuring transparency. We all share a stake in the effectiveness of the stimulus funds and ensuring that they are appropriately targeted and spent. I believe that our State Department of Education is at work on form that will ensure that reporting requirements are met and districts are not overburdened administratively. It is especially important that smaller school districts not be given reporting requirements that overwhelm their administrative capacity.

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<sup>10</sup> U.S. Department of Education, *Guidance: Funds under Title I, Part A of the Elementary and Secondary Education Act of 1965 Made Available under the American Recovery and Reinvestment Act of 2009*, April 2009, p. 28.

**Involvement of Educators**

In order to make all of this work, and ensure that the funds provided under ARRA are used efficiently and in a coherent and coordinated manner, it is critical that the Governor and Commissioner work closely with CEA and that district superintendents work closely with our local affiliates. Ensuring that classroom educators have a voice in the process for determining the best use of the funds and are involved in the implementation and evaluation of programs and services that are paid for with these funds, will increase the chances that the ARRA funds achieve their twin goals of creating and saving jobs, on the one hand, and advancing education reforms, on the other hand.

**Conclusion**

The overall result of almost \$800 million in new federal education funding for our state is unreservedly positive and we again commend Congress and the President for their historic support for education. Without a doubt, education would have been funded less well without the ARRA. How much less would have been provided to it is difficult to determine with any precision.

We believe that the promise of ARRA is great. A Congressional Research Service report notes that "in 2010, CBO projects that the ARRA would boost ... employment by a range of 1.2 million to 3.6 million in 2010 compared to what it otherwise would have been."<sup>11</sup>

As noted in this testimony, however, it is our strong conviction that in order to achieve the upper bounds of the CBO's estimate, creativity and flexibility will be necessary. The Connecticut education context I have shared with you today is but one example of what could be achieved with these stimulus funds. On behalf of the CEA and the NEA, we very much appreciate your effort to hear our stories and to work with us toward economic recovery.

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<sup>11</sup> Congressional Research Service, *Economic Stimulus: Issues and Policies*. 2/27/09 P. 10



**TESTIMONY OF**  
**STEPHEN FRAYNE**  
**SENIOR VICE PRESIDENT, HEALTH POLICY**  
**CONNECTICUT HOSPITAL ASSOCIATION**  
**BEFORE THE**  
**U.S. SENATE COMMITTEE ON HOMELAND SECURITY**  
**AND GOVERNMENTAL AFFAIRS**  
**Tuesday, April 7, 2009**

**The American Recovery and Reinvestment Act:**  
**Making the Economic Stimulus Work for Connecticut**

My name is Stephen Frayne. I am the Senior Vice President, Health Policy, of the Connecticut Hospital Association (CHA). I appreciate the opportunity to testify on how the funds provided by the American Recovery and Reinvestment Act of 2009 will help Connecticut communities – in particular my testimony will focus on how those funds can best be used to help Connecticut hospitals.

Connecticut hospitals are more than facts and figures and dollars and cents – Connecticut hospitals, at their core, are really people taking care of people. Each year the more than 66,000 people employed in Connecticut hospitals work hard to provide the patients they serve with the very best care. Providing patients and communities with the finest quality healthcare services is the highest priority for Connecticut's not-for-profit hospitals. Hospitals fulfill a vital role, caring for Connecticut residents 24 hours a day, seven days a week, and they make enormous contributions to the health and quality of life for millions of Connecticut residents. Last year, Connecticut hospitals provided 2.1 million days of inpatient care and more than 4 million outpatient visits, including 1.5 million emergency department visits, 179,000 ambulatory surgery visits, 31,000 cardiac procedures, 94,000 cardiac rehab visits, 153,000 gastroenterology procedures, 46,000 chemotherapy visits, 192,000 radiation therapy visits, 804,000 outpatient rehabilitation visits, 332,000 psychiatric care visits, and 623,000 primary care visits. Every moment of every day, hospitals touch the lives of Connecticut residents by providing high quality healthcare services.

Hospitals also make vital contributions to the state's economy. Connecticut's hospitals are both the economic bedrock and engine in their communities. They are major employers, offering jobs at all skill and salary levels in a growing employment sector. Connecticut hospitals won't move out of Connecticut in search of a more favorable business climate – Connecticut hospitals are here to stay. Hospital purchases provide important secondary income and job benefits to the local economy. Hospitals serve as a magnet for other healthcare business and serve as a stimulus for economic development, attracting other businesses into the community, such as retail shops, banks, grocery stores, and family restaurants. CHA analysis of the economic impact of Connecticut hospitals shows Connecticut hospitals and health systems:

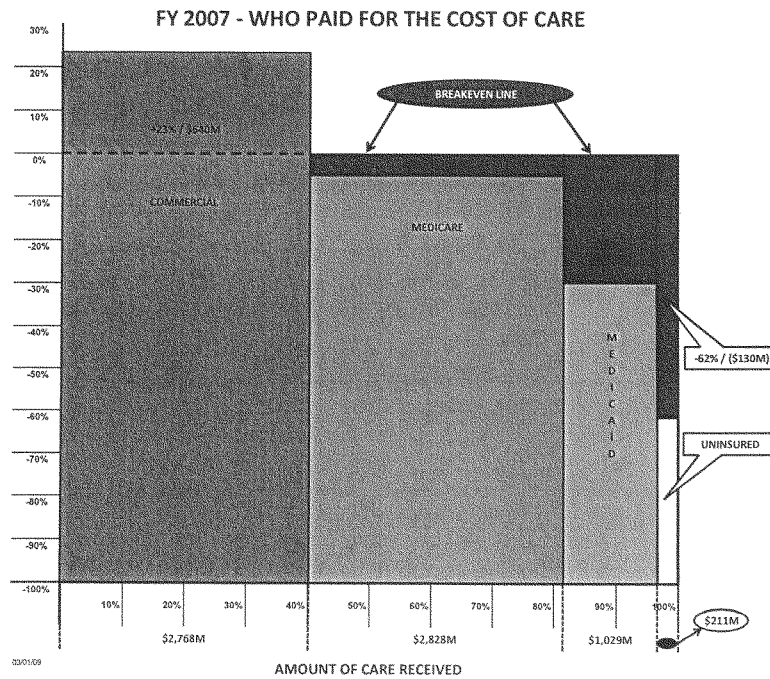
- Generate nearly **\$12.8 billion** per year for the state and local economies;
- Provide **97,000** jobs in our communities generating approximately **\$7.0 billion** in annual local economy payroll; and

- Purchase goods and services generating approximately **\$5.8 billion** annually in local economic activity.

During the last four years, there has been a 31% increase in hospital contributions to Connecticut's economy—from \$9.8 billion in 2004 to \$12.8 billion in 2007.

In more ways than one, the health of our communities is inextricably linked to the health of their local hospitals. In the best of times, the ability of Connecticut hospitals to continue to provide the highest quality care and to make contributions to the broader Connecticut economy is constantly threatened. Payments for individuals enrolled in state and federal programs always fall short of the amount needed to cover the cost of care. These deficits rob Connecticut hospitals of the dollars needed for investment in staff, facilities, and acquiring modern technology.

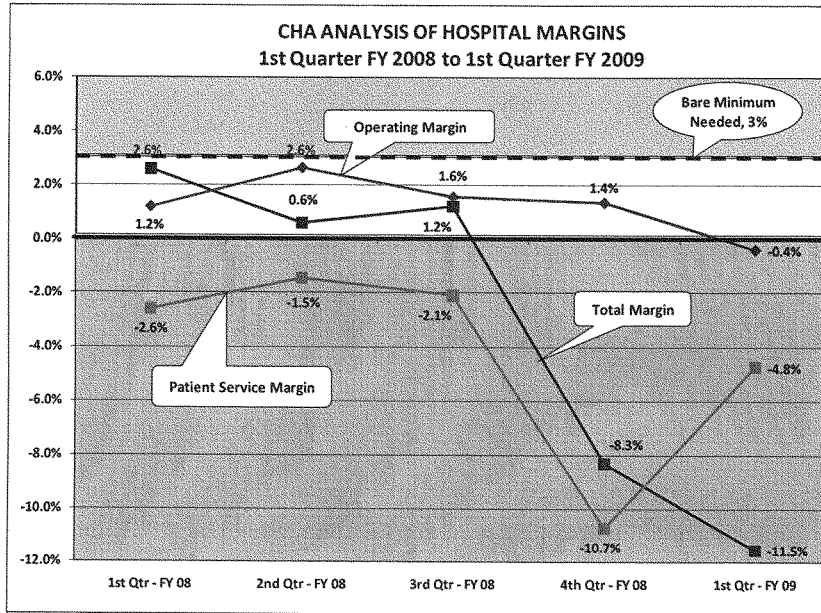
As the chart below clearly indicates, every year, before a hospital plans a new program, hires another nurse, or invests in a quality initiative, it must figure out how to cover the annual \$564 million deficit caused by state and federal government underfunding as well as providing services to those who are uninsured. This challenge is never ending and the gap is ever growing, causing Connecticut hospitals to have to annually implore the state and the federal governments for help.





The constant pressures of inadequate government funding, the need to attract and maintain a superior workforce, rising input costs, and the continuous effort to improve the care given have put Connecticut's hospitals in the best of times in a financially tenuous position. Unfortunately, these are not the best of times; at this point, 2007 looks like "the good old days."

As the table below indicates, contrary to popular belief, hospitals are not recession-proof. The economic crisis is ravaging the health of our hospitals. In 2008, one of the traditional means hospitals use to make ends meet—non-operating (investment) income—more than disappeared, going negative for the first time ever. Instead of investments supporting operations, hospitals posted a non-operating revenue loss of over \$200 million. In comparison to the year before, this represented a year-over-year nose dive in non-operating revenue of \$416 million. Unfortunately, the slide from the end of 2008 has continued unabated into the first quarter of 2009. In the first quarter of 2009, hospitals lost another \$200 million. We have never seen results as bad as these.



However, not all the news is bad. Thankfully, with your leadership, Senator Lieberman, Congress is delivering through the stimulus package much needed relief. I am going to focus the balance of my comments on four areas: 1) the increase in funding for the Medicaid program through enhanced federal match; 2) the increase in hospital funding to care for the uninsured; 3) the increase in Medicare hospital funding for meaningful adopters of electronic health records; and 4) the availability of a federal match of 5-to-1 for states that create a loan program for providers wishing to borrow funds to implement electronic health records.

The enhanced federal match for Medicaid offers Connecticut much needed relief. This relief will come in the form of an increase in Connecticut's match rate from the current 50 percent to about 60 percent. The relief is estimated to total over \$1.32 billion through December 2010. Sadly, even with this enormous relief it is unlikely any of it will reach providers; options before the legislature range from at best a rate freeze for two years to Medicaid funding cuts totaling about \$170 million over the next two years. Some of the proposed cuts are:

- Imposing co-payments in the Medicaid program
- Establishing premiums for HUSKY A Adults
- Eliminating self-declaration at application and redetermination
- Modifying the definition of medical necessity and appropriateness under Medicaid
- Eliminating state-funded non-emergency medical assistance to non-citizens
- Limiting the dental services benefit for adults to emergencies
- Increasing premium payment requirements under HUSKY B
- Eliminating supplemental payments to FQHCs and hospitals for prenatal care when the mother is undocumented
- Eliminating medical interpreters under Medicaid
- Eliminating funding for the LIFE STAR helicopter

Given the size of the congressional lifeline, Medicaid funding should be enhanced, not reduced. Medicaid funding should be used first and foremost to absorb the growing numbers seeking eligibility, maintain coverage, and make another down payment on bringing provider rates closer to covering the cost of care. In other words, use Medicaid funding for Medicaid and help those who need it most, support those providing the help, and then use the balance, which will likely exceed \$1.1 billion dollars, to contribute to balancing the state budget. In these difficult economic times, it is more important than ever that we remain steadfast in our commitment to help those who cannot help themselves. If we use the funds in this way, rather than just to plug the state deficit, we would create over 2,800 Connecticut jobs, provide \$1.1 billion to the general fund, increase economic activity in the Connecticut general economy by about \$350 million per year, and increase Connecticut salaries and wages by over \$125 million per year.

Section 5002 of the American Recovery and Reinvestment Act offers states the ability to ensure access to healthcare for the uninsured by covering the costs of that care at hospitals. Eligible hospitals are those that serve a disproportionate share of low-income or uninsured individuals and are known as Disproportionate Share Hospitals (DSH). In Connecticut, every hospital in the state is eligible. The Recovery Act increases the amount of funding available for Connecticut hospitals by about \$5 million per year for the next two years. Unfortunately, Connecticut hospitals will not receive any additional funds to take care of the growing number of uninsured – because to receive those funds, states must first spend DSH funds that are already available. Connecticut does not use all the DSH funds already available to it.

Section 4102 of the American Recovery and Reinvestment Act of 2009 sets forth a Health Technology Medicare Incentive Payment for hospitals. As the table below indicates, Connecticut hospitals are likely to receive almost \$150 million dollars over four years if they are able to demonstrate "meaningful use" of electronic health records. If a hospital qualifies for this incentive payment, the hospital will receive payments beginning in Federal Fiscal Year (FFY) 2011 that will continue and phase out over four years. Hospitals that do not qualify by FFY 2015 will not receive any incentive payments. Beginning in FFY 2015, hospitals that do not qualify as meaningful users of EHR will be penalized with a reduced market basket update to their Medicare payment rates. These reductions will be transitioned in over three years such that by FFY 2017, three-quarters of the market basket will be held back if a hospital does not qualify.

**CHA Estimate of American Recovery and Reinvestment Act of 2009  
Medicare Health Information Technology Incentive Payments**

<b>Hospital Name</b>	<b>First Year Payment</b>	<b>Second Year Payment</b>	<b>Third Year Payment</b>	<b>Fourth Year Payment</b>	<b>Maximum HIT Funding Available</b>
The William W. Backus Hospital	1,949,854	1,462,391	974,927	487,464	4,874,636
Bridgeport Hospital	2,622,483	1,966,862	1,311,241	655,621	6,556,206
Bristol Hospital	1,642,537	1,231,903	821,269	410,634	4,106,343
Hospital of Central Connecticut	3,239,908	2,429,931	1,619,954	809,977	8,099,770
Connecticut Children's Medical Center	-	-	-	-	-
Danbury Hospital	3,180,707	2,385,531	1,590,354	795,177	7,951,768
Day Kimball Hospital	1,505,871	1,129,403	752,935	376,468	3,764,676
John Dempsey Hospital	1,314,760	986,070	657,380	328,690	3,286,900
Greenwich Hospital	1,737,784	1,303,338	868,892	434,446	4,344,461
Griffin Hospital	1,805,863	1,354,398	902,932	451,466	4,514,659
Hartford Hospital	3,004,672	2,253,504	1,502,336	751,168	7,511,679
The Charlotte Hungerford Hospital	1,689,681	1,267,261	844,840	422,420	4,224,202
Lawrence & Memorial Hospital	2,301,961	1,726,470	1,150,980	575,490	5,754,901
Manchester Memorial Hospital	1,673,258	1,254,944	836,629	418,315	4,183,146
Middlesex Hospital	2,400,204	1,800,153	1,200,102	600,051	6,000,511
MidState Medical Center	2,175,585	1,631,689	1,087,792	543,896	5,438,962
Milford Hospital	1,371,716	1,028,787	685,858	342,929	3,429,289
New Milford Hospital	1,276,928	957,696	638,464	319,232	3,192,319
Norwalk Hospital	2,715,704	2,036,778	1,357,852	678,926	6,789,261
Rockville General Hospital	1,372,186	1,029,139	686,093	343,046	3,430,465
Saint Francis Hospital And Medical Center	3,009,170	2,256,878	1,504,585	752,293	7,522,925
Saint Mary's Hospital	2,297,863	1,723,397	1,148,932	574,466	5,744,658
Hospital of Saint Raphael	3,766,731	2,825,048	1,883,365	941,683	9,416,827
St. Vincent's Medical Center	3,020,892	2,265,669	1,510,446	755,223	7,552,230
The Stamford Hospital	2,322,672	1,742,004	1,161,336	580,668	5,806,679
Waterbury Hospital	2,483,274	1,862,456	1,241,637	620,819	6,208,185
Windham Community Memorial Hospital	1,594,908	1,196,181	797,454	398,727	3,987,270
Yale-New Haven Hospital	2,123,721	1,592,790	1,061,860	530,930	5,309,302
<b>State Total</b>	<b>59,600,89</b>	<b>44,700,669</b>	<b>29,800,446</b>	<b>14,900,223</b>	<b>149,002,230</b>

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Finally, section 3014 of the American Recovery and Reinvestment Act offers competitive grants to states for the development of loan programs to facilitate the widespread adoption of certified electronic health record technology. No one disputes the need to convert to electronic health records or the quality and cost saving advantages that will accrue as a consequence of such conversion. So what is taking so long to get it done? Converting to electronic health records is a time consuming, complex, and very expensive undertaking, which will take years to complete and will cost into the tens of millions of dollars per hospital. Given the potential for cuts in Medicare funding if we do not succeed in implementing electronic health records, it is critical that hospitals have access to capital at reasonable rates. We are talking to members of the administration and legislative leaders about the necessity to take advantage of this critically-needed program and are cautiously optimistic that it will be pursued.

Hospitals are in a very difficult spot, being challenged past the breaking point in today's environment. The numbers of uninsured and those enrolling in Medicaid are rapidly growing. Current input costs, like staff, extraordinary pension funding expense, drugs, implants, fuel, and power to name a few, are rising. New costs, like electronic health records, are being added. Revenue to cover these demands is at best flat and the value of other assets to cover losses is down sharply. The confluence of these challenges and the speed at which they are being hurled at hospitals is unprecedented and is taxing the ability of hospitals to deliver excellent patient care with the best staff in modern facilities with the latest equipment.

Yet, many of the resources available to help meet these challenges lie just beyond the reach of hospitals; access to these resources is dependent on others willing to help hospitals and other providers. Absent the State legislature and the administration acting affirmatively, all of the additional Medicaid funding will flow to balance the state budget and none will go to hospitals or other providers; hospitals will not be able to access the increased DSH funding available to care for the growing number of uninsured; and, hospitals and other providers will not be able to access a loan program so that we can have the funds to proceed with electronic health record implementation.

Thanks to your hard work, before us we have some unprecedented opportunity – which we cannot afford to squander. We hope the legislature and the administration will work together to use some of the Medicaid funds to help providers make ends meet, access the additional DSH funds to help hospitals cover the growing number of uninsured, and pursue the electronic health record loan program. I would be happy to answer any question you might have.

Thank you for your consideration of our views.

**CONNECTICUT  
VOICES  
FOR CHILDREN**

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**Testimony of Sharon D. Langer, Senior Policy Fellow  
Field Hearing of the U.S. Senate Committee on Homeland Security and Governmental  
Affairs  
The American Recovery and Reinvestment Act: Making the Economic Stimulus Work  
for Connecticut  
April 7, 2009**

Chairman Lieberman, Ranking Member Collins, and Members of the Committee:

I am honored to present testimony today on behalf of Connecticut Voices for Children, a research-based public education and advocacy organization which works statewide to promote the well-being of Connecticut's children, youth, and families. Thank you for inviting me here this morning to discuss the challenges that our state faces in ensuring that the stimulus funds for health care and education are spent quickly, wisely and fully.

I provide this testimony from the vantage point of our organization's understanding of the Medicaid program and educational systems, in particular, and our work on broader issues related to how we fund government and how we spend our federal and state revenues. We at Connecticut Voices are fortunate to have on staff individuals who have varied backgrounds and advanced degrees in law, education, economics, public health, public policy, and social work.

We know that our state is reeling from the collapse of the financial markets, the slump in the housing market, and the alarming increase in the unemployment rate – now 7.4%. At the same time the Governor and the state legislature are faced with tackling a projected state budget deficit of \$8 billion over the next two state fiscal years starting July 1<sup>st</sup>. Our current yearly services budget is \$18 billion. Connecticut's 169 cities and towns in turn are faced with terrible budget choices. The federal stimulus dollars have come none too soon to help our state keep its commitment to children and struggling families.

Connecticut is slated to receive approximately \$3 billion in new federal dollars through the American Recovery and Reinvestment Act (ARRA) in order to preserve essential services and to assist our state in saving and creating new jobs during this deep economic recession. Of the \$3 billion, Connecticut expects to receive \$1.32 billion in additional Medicaid funding during the 27 months covered by the stimulus package – October 1, 2008 through December 31, 2010, and over \$500 million in federal educational stabilization funds.

We are heartened to see that federal government agencies, such as the Centers for Medicare and Medicaid Services (CMS) within the U.S. Department of Health and Human Services, and the U.S. Department of Education have already begun to issue guidance to the states on how to take full advantage of the funding opportunities of the stimulus and also comply with the maintenance of efforts provisions, and the stringent reporting and accountability requirements. For instance, the CMS guidance precludes adoption of the Governor's recommendations to impose premiums on low-income parents receiving Medicaid or eliminate simplified application processes that have helped families get on Medicaid more quickly and therefore access need care sooner. Adoption

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53 Oak Street, Suite 15 • Hartford, CT 06106 • Phone 860-548-1661 • Fax 860-548-1783 | E-mail: [voices@ctkidslink.org](mailto:voices@ctkidslink.org)

of such budget “savings” measures would violate the Medicaid maintenance of effort requirements, and jeopardize our state’s ability to access the additional Medicaid funds under the stimulus. The legislature’s appropriations committee budget rejects the Governor’s recommendations, as well as many others that would reduce health care services to over 450,000 low-income children, families, seniors and persons with disabilities, who rely on our Medicaid program. We would have to cut almost 3 dollars in health care to save a dollar in state funding during the next two years to garner “savings” in Medicaid.

We know that the Obama Administration through conference calls, postings on the federal [www.recovery.gov](http://www.recovery.gov) and agency websites, and other outreach efforts, is attempting to communicate quickly and clearly with the many government and non-government stakeholders about what is in the stimulus, and how to take full advantage of the opportunities the new law presents.

We are worried, however, that Connecticut will forego opportunities to utilize all the federal funds available since the state has a long history of leaving federal funding on the proverbial table – whether they are funds for Medicaid, Disproportionate Share Hospital payments, the Children’s Health Insurance Program, or others, and because of the opaque nature of Connecticut’s budgeting process.

With regard to the State Fiscal Stabilization Fund Program (SFSFP), there will be many challenges to ensure that the money reaches local school systems in time to prevent layoffs and the reduction of essential services to vulnerable children. The detailed Guidance on the SFSFP issued at the end of this past week lays out the steps that states must take in order to receive the funds.

#### **Connecticut’s state budgeting process will make it difficult to know how federal stimulus dollars are spent**

Connecticut “gross budgets” federal Medicaid and child welfare (“Title IV-E”) dollars, and appropriates many of the federal block grant funds. This means that the federal and state dollars are combined in line items of the state budget. For example, the anticipated Medicaid stimulus funds in the form of increased federal medical assistance percentage (FMAP) payments to the state will appear in the “Medicaid” line item in the state Department of Social Services budget. As a result of this longstanding practice of including the federal funds without explanation in the state budget, it will be difficult to track the actual use of the federal stimulus funds. With regard to federal grant funds, the legislature’s Office of Fiscal Analysis lumps all federal grant funds together in each agency’s budget without explaining which general fund or other appropriate fund programs are receiving the federal monies.

Shelley Geballe, Distinguished Senior Policy Fellow, and co-founder of Connecticut Voices for Children, has submitted recommendations to our state legislature about requiring greater detail in the Governor’s budget with regard to the appropriation of federal funds received via federal matching programs, such as Medicaid and Title IV-E, as well grant funded programs.

To meet the transparency and accountability goals of the ARRA our organization has urged the legislature to require that the Governor report how ARRA funds have been incorporated within the state budget in FY 09, FY 10, and FY 11, including

- The total amount of ARRA funds included in each budget line of the General Fund budget; and
- The specific uses to which ARRA funds have been used or are proposed to be used in each fiscal year.

While we support state legislation to convene a state Commission on Federal Stimulus Distribution (Senate Bill 246), your Committee may be interested in the following recommendations Attorney Geballe made to the state legislature to maximize the effectiveness of such a Commission:

- the Commission should be constituted quickly and hold meetings at least monthly;
- the Governor should be required to provide bi-weekly reports to the Commission on her current efforts to respond to the various deadlines, requirements, and competitive grants in the ARRA; and
- the agendas and minutes of the Commission and the Governor's bi-weekly reports to the Commission be posted on Connecticut's ARRA "recovery" website ([www.recovery.ct.gov/recovery/site/default.asp](http://www.recovery.ct.gov/recovery/site/default.asp)).

The implementation timeline for the ARRA is understandably quite rapid. Establishing the Commission and requiring public reporting of all current efforts to draw down and use ARRA funds would increase markedly transparency and accountability in the use of ARRA funds, a key goal of the federal legislation. It also would help ensure that the funds are put to their highest and best use, and provide the federal government with a window on the state's plans for distribution of the funds.

Thank you for this opportunity to provide testimony today on the implementation of the ARRA in Connecticut. Please feel to contact me or my colleagues at Connecticut Voices for Children if you need further information.

**Prepared Statement of  
Elliott C. Nelson  
Chairman, Bristol Democratic Town Committee**

Senator Lieberman & members of the Senate Committee on Homeland Security and Governmental Affairs,

I heard Senator Lieberman speak at length about Health Information Technology with panelist Stephen Frayne from the Connecticut Hospital Association during the field hearing in Connecticut. I just wanted to reiterate how important that is to our society. I am the Democratic Town Chairman in Bristol, but I have also been a firefighter for the City of Bristol over the past 26 years. As a first responder, I know how vital every second can be in an emergency situation. Having an electronic database in our healthcare system could greatly improve the seconds spent working on a patient when they come into a hospital. Imagine having someone come in, and within seconds knowing their medical history, and what medications they may be allergic to, and their family contact information. This could greatly change our healthcare system and improve the quality of care that patients receive when they enter into a medical facility.

Health Information Technology could also open up a whole new infrastructure for jobs and communication among our citizens. As someone in the political field, I know that we have electronic databases for our registered voters, but they are very hard to maintain with the limited staff that we have funds available for. A health information technology system would require constant monitoring for accurateness and electronic threats such as hackers, and would also require outreach to make sure that as many people as possible are entered into the system. This could also help the medical field in getting educational information out to certain populations affected by certain chronic diseases. The uses for this information are endless, although I'm sure we will put some limits on it along the way.

We need to find a way to make sure that as many cities, towns, and states for that matter, take advantage of the HIT benefits built into the stimulus package. Money has to be spent for money to be received, but I think it is well worth the advantages we will all get out of this to spend the money even in these hard economic times. A healthcare system with an electronic database could be more focused on prevention and the quality of interactions instead of the quantity of them. This in the end could save us money on many levels, which is why I feel it is important to spend the money even now.

Thank you for allowing attendees of the event to submit testimony to your committee. It shows your dedication to getting the input of the taxpayers on where they want their money to go, and to getting the true story of what is happening with our federal stimulus dollars.

Submitted by:

Elliott C. Nelson  
Chairman, Bristol Democratic Town Committee



**Prepared Statement for Chairman Joseph Lieberman**  
**“Follow the Money: State and Local Oversight of Stimulus Funding”**  
**Washington, DC**  
**April 23, 2009**

Good morning and welcome to this fourth in a continuing series of hearings this Committee will hold on the American Recovery and Reinvestment Act to monitor how effectively and efficiently the money is being spent and make sure it is doing the job we intended it to do – breath life back into the economy.

Since we are barely 60 days into the stimulus package, it’s hard to draw any firm conclusions, but I think the initial signs are hopeful on both counts.

As of mid-April, nearly \$60 billion has already been made available for grants and projects that are putting people to work and giving a boost to local economies.

That’s about \$1 billion a day – an astounding figure, but the kind of jolt a \$14 trillion economy needs to get moving again and save or create 4 million jobs.

Also, 2,400 transportation construction projects have been approved in all 50 states, with \$7.5 billion already out the door and more expected to be contracted as the spring and summer construction season kicks off.

This will not only create jobs but leave us with a stronger system of roads, rails and bridges that will itself be an aid to the economy when we come out of this recession.

But the speed of spending is as important as the amount if the stimulus is to be effective. That \$60 billion figure represents about 12 percent of the nearly \$500 billion in non-tax relief stimulus funds, which puts us ahead of schedule to meet our goal of spending 70 percent of those funds by the summer of 2010.

Besides the money targeted to direct spending, 110 million Americans are getting \$27 billion in direct tax relief through the Making Work Pay tax credit in their paychecks. That’s extra money for 95 percent of all families.

While I know it’s too soon to draw conclusions, I believe we are seeing glimmers of hope in the economy. March was the best month for the stock markets in years.

According to the Vice Chairman of the Federal Reserve, consumer spending seems to be steady and contraction of the housing market has slowed.

In my home state of Connecticut, a survey of small businesses reported that they were finding it easier to get the credit they need to make payroll and finance inventory.

But unemployment – now at 8.5 percent – is expected to rise to more than 10 percent and it will take time to bring that down to full-employment levels again.

If we get the Recovery Act right, along with the other efforts being pursued by the Federal Reserve and the Treasury, we will stabilize the system and restore confidence so that the private sector can once again start creating new jobs.

I look forward to this morning's testimony from Acting Comptroller General Gene Dodaro of the Government Accountability Office as he presents GAO's first report on State and local spending as required by the Recovery Act.

We also will hear reports from the front lines from Mr. Ray Scheppach of the National Governors Association and Ms. Carolyn Coleman of the National League of Cities.

As impressive as the amounts distributed to date are, most of the stimulus money has yet to hit the street. Much of the work of state and local governments right now is in preparing to comply with the rules governing applying for, implementing and monitoring stimulus spending.

Remember that the Recovery Act imposes rigorous new requirements for accountability and transparency of stimulus funds. Officials at all levels of government are being asked to do more – and in record time.

Last week we held a field hearing in Connecticut and the state Secretary of Policy Management testified that the federal government has reacted swiftly to answer questions and keep red tape to a minimum.

However, during that hearing we learned that important implementation challenges exist. In particular, we need to give the state and local government's clear direction on whether some of the Recovery Act money can be used to help pay for administrative and oversight costs.

The Recovery Act included \$250 million for federal inspectors general to hire experienced auditors and investigators for their agencies.

But about \$300 billion of the stimulus spending will be under the supervision of cash-strapped state and local governments that may be forced to lay off the very personnel needed to oversee Recovery Act spending so we can avoid the kinds of waste, fraud, abuse or theft that could discredit the program.

Vice President Biden has assured Sen. Collins and me that his office is working on this and has sent a letter to that effect that I will later place into the record.

But, I am particularly pleased that in the letter the Vice President has committed to issuing new guidance through OMB that will give new flexibilities for States to cover administrative costs associated with the Recovery Act.

In addition, I also want to note that there will be a week-long national on-line forum beginning Monday on the Recovery.gov web site on technology solutions to improve the monitoring of Recovery Act funds.

This will be an excellent opportunity for the public, potential recipients, state and local governments, and IT companies to weigh in on how the web site should be set up. I look forward to hearing the results of that dialog.

Another problem I see is the need to bring harmony to the twin goals of the Recovery Act -- the immediate goal of saving jobs and rejuvenating the economy but also bringing about major reforms to our education and health care information systems.

I liken it to a leaky dike. You can stick your fingers into the leaks to keep the dike from collapsing but now your hands are busy and you can't do what you really need to do -- build a new dike.

We heard about this during our hearing in Connecticut, especially regarding the education reforms that are part of the Recovery Act. School districts that are just scraping by will find it a challenge to meet the reforms envisioned by the Recovery Act while trying to avoid major layoffs.

But those education reforms, which I support, are ultimately crucial to the putting the economy back on a sound, long-term footing by giving our children an education that will allow them to grow up and compete with young men and women from any nation in the world.

I look forward to hearing GAOs testimony on how effective the Recovery Act has been to date and how we solve some of the questions I've just raised.

**Statement of  
Senator Susan M. Collins**

**'Follow the Money: State and Local Oversight of Stimulus Funding'**

**April 23, 2009**

The American Recovery and Reinvestment Act is vital legislation intended to boost our troubled economy and create jobs. If properly implemented and overseen, the law will improve our nation's roads and bridges, prevent cuts in health care, and provide important investments in education and science, while helping to turn our economy around.

State and local governments will play a critical role in distributing, spending, and measuring the impact of Recovery Act funds. GAO estimates that state and local programs will receive about \$280 billion. As a result, they must prepare themselves to handle the challenge of managing and overseeing these funds – a resource-intensive undertaking. This challenge is further compounded by the fact that many state and local governments are also facing major budget shortfalls that often leave them short-staffed.

The Recovery Act creates several important oversight mechanisms, including bi-monthly reports from the Government Accountability Office on the use of funds by selected states and localities. GAO is issuing its first of these reports today. We are eager to hear from GAO on the progress that state and local governments have made in developing plans and internal controls to ensure that Recovery Act funds are not lost to waste, fraud, and mismanagement.

Today's hearing will also explore the mandates for accountability and transparency placed on state and local governments by the Recovery Act.

I am pleased to welcome the National Governors Association and the National League of Cities to this hearing. These associations can provide useful insight into the innovative approaches state and local governments are taking to implement the Recovery Act, including how they plan to communicate funding opportunities to hospitals, fire departments, companies, schools, and non-profit organizations, to award infrastructure contracts effectively, and to ensure that taxpayer dollars are not wasted.

**Homeland Security and Government Affairs Committee**  
**Statement of Sen. Michael F. Bennet**  
**“Follow the Money: State and Local Oversight of Stimulus Funding”**  
**April 23, 2009**

Thank you Mr. Chairman for conducting this important hearing. It's Congress's job to make sure investments intended to jumpstart this economy are wise and managed properly. Americans need a reason to shake off their disappointment in Washington. We have new leadership; and a new opportunity. We must do better. The time is now.

In Colorado and across the nation – the recovery package is beginning to create jobs. The investments we are making in our roads, bridges, highways, health care, energy and education are sound investments. But we must try to steward every last dime. America cannot afford waste, fraud or abuse.

I traveled to 14 counties while Congress took its Easter break. I heard from Coloradans who are struggling. Coloradans are on the front lines combating soaring joblessness, rising health care costs, and an education system that is failing far too many kids.

The unemployment rate reached 7.5% last week in Colorado. People looking for work in this job market are fighting an uphill battle. Our communities must come together to help them during this tough time.

But more importantly to our future, we must use this moment to reinvest in the sectors which will drive job creation. This means green jobs, high-wage infrastructure jobs, disease research and technology training. The middle class will benefit most from these investments. And we must always remember that our middle class is our greatest resource.

Passing the rescue package does not end Congress's work. We must ensure that states and localities receive the funds quickly, efficiently, and appropriately. We must get the

word out -- middle class families need to know about the tax credits and tax cuts that are available to them.

And we must work to prevent abuse of these newly available funds. Where we find that someone has tried to defraud the government, we must swiftly investigate, prosecute and punish.

The only way to conduct proper oversight is to work together. For Colorado, that means our congressional delegation working with our Governor. And it means government at all levels working with the private sector. Communication and information sharing are key.

Oversight is about getting the details right. Congress must earn its keep -- protecting the money that is supposed to be working for the American people.

This GAO Report is mostly very encouraging news. But just as more and more Americans will bounce back as they utilize rescue resources, potential wrongdoers will get more sophisticated in their attempts at abusing the system too. We have to keep after oversight. We must engage local, state and federal officials so if and when there's a problem, we're on top of it and not caught flat-footed.



THE VICE PRESIDENT  
WASHINGTON

April 23, 2009

The Honorable Joseph I. Lieberman  
Chairman  
Committee on Homeland Security and Governmental Affairs  
United States Senate  
Washington, D.C.

The Honorable Susan M. Collins  
Ranking Member  
Committee on Homeland Security and Governmental Affairs  
United States Senate  
Washington, D.C.

Dear Chairman Lieberman and Ranking Member Collins:

Thanks to your leadership, just over sixty days after Congress passed the American Recovery and Reinvestment Act (ARRA), it is already providing immediate financial relief for American families and funding billions of dollars in new projects that are creating jobs, strengthening local economies and building a strong foundation for our economic recovery.

Because of your support:

- Ninety-five percent of working families have begun to see the benefit of the Making Work Pay tax credit in their paychecks.
- Unemployed individuals are collecting an extra 25 dollars a week in unemployment benefits and paying 65% less for group health benefits through COBRA.
- More than 2,400 transportation construction projects have now been funded in all fifty states.
- Stimulative spending is ahead of schedule with more than \$75 billion in Recovery Act funds already made available for specific grants and projects.

The President has asked me to oversee the Recovery Act, a responsibility I take particularly seriously given the size and scope of the law. I am not alone in providing this oversight. The Recovery Act established the Recovery Accountability and Transparency Board and also gave the Government Accountability Office (GAO) significant responsibilities in this area. To ensure that Recovery Act implementation meets the highest standards of accountability and transparency, I recommended Earl Devaney, a former Secret Service agent and Interior Department Inspector General, to chair the Board. My staff and I are in constant communication

with both Mr. Devaney and GAO to ensure that oversight efforts are coordinated and avoid overburdening the recipients of Recovery Act funds.

Recently, the Acting Comptroller General and I met to discuss reports GAO was preparing pursuant to their responsibility under the Recovery Act. We welcome this dialogue with GAO and look forward to building on the observations from their field work, as well as their overall insights. I have also been reaching out to governors and local officials on a weekly basis to solicit their feedback on what more we might be doing to implement the Act. Many of the items GAO discusses also have been raised by the governors and local officials. To address these concerns, I asked OMB Director Peter Orszag to review their current guidance and see where it might be supplemented.

As you know, the Office of Management and Budget (OMB) has issued two guidance documents on Recovery Act implementation on February 18, 2009 and April 3, 2009. OMB is preparing additional rounds of guidance which are currently being discussed with Federal agencies, state and local governments, and other potential recipients. OMB will begin issuing updated guidance in early May that will address several points that GAO has touched on as well as concerns from state and local officials. Allow me to summarize some of the areas of guidance here:

- Additional detail on data reporting requirements, including data definitions, formats, and methods of transmission
- Roles and responsibilities of recipients and sub-recipients with respect to data collection, data quality, and other compliance and performance issues associated with the Recovery Act
- New flexibilities for states for costs of administrative activities associated with the Recovery Act
- Changes to the single audit process to ensure Recovery Act activities receive special emphasis and audit scrutiny
- A standard procedure for recipients to calculate jobs created

This guidance will be issued in final form but, as they have done in the past, OMB will welcome questions and comments.

Our work with the Recovery Board is also proceeding in the area of solution development for reporting. OMB has responsibility for establishing the policies that ensure timely and reliable data is obtained from Federal agencies and recipients. The Board has responsibility for determining how best to present that data on Recovery.gov so that the public has transparency into the who, what, where, and how of Recovery Act funding.

Beginning April 27<sup>th</sup>, Recovery.gov will host a week-long national online forum, Recovery Dialogue on Information Technology Solutions, to engage the public, potential recipients, solution providers, and state, local and tribal partners in developing more effective tools for public monitoring of Recovery Act funds. Information from the online event will be used to inform procurement decisions and improve communication going forward with both key stakeholders and the public at large.

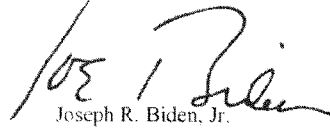


*Letter to Chairman Lieberman and Ranking Member Collins- Page 3*

I look forward to working with you as we continue these and other efforts to ensure Recovery Act funds are moving promptly and in full transparency toward the projects and programs that will most effectively drive our economic recovery.

Again, I would like to thank you for your support and to encourage you to contact me with any questions you may have.

Sincerely,

A handwritten signature in black ink, appearing to read "Joe Biden".

Joseph R. Biden, Jr.

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**GAO**

United States Government Accountability Office

Testimony  
Before the Committee on Homeland  
Security and Governmental Affairs, U.S.  
Senate

For Release on Delivery  
Expected at 9:00 a.m. EDT  
Thursday, April 23, 2009

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## RECOVERY ACT

### As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues Is Essential

Statement of Gene L. Dodaro  
Acting Comptroller General of the United States



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GAO-09-631T

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Mr. Chairman, Ranking Member Collins, and Members of the Committee:

I am pleased to be here today to discuss our work examining the uses and planning by selected states and localities for funds made available by the American Recovery and Reinvestment Act of 2009 (Recovery Act).<sup>1</sup> The Recovery Act is estimated to cost about \$787 billion over the next several years, of which about \$280 billion will be administered through states and localities. Funds made available under the Recovery Act are being distributed to states, localities, and other entities and individuals through a combination of grants and direct assistance. As you know, the stated purposes of the Recovery Act are to:

- preserve and create jobs and promote economic recovery;
- assist those most impacted by the recession;
- provide investments needed to increase economic efficiency by spurring technological advances in science and health;
- invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits; and
- stabilize state and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

As I described in my March testimony,<sup>2</sup> the Recovery Act specifies several roles for GAO including conducting bimonthly reviews of selected states' and localities' use of funds made available under the act.<sup>3</sup> My statement today is based on our report being released today, *Recovery Act: As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues Is Essential*, which is the first in a series of bimonthly reviews we will do on states' and localities' uses of Recovery Act funding and covers the actions taken under the Act through April 20, 2009.<sup>4</sup> Our report and our other work related to the Recovery Act can be found on our new website called *Following the Money: GAO's Oversight of the Recovery Act*, which is accessible through GAO's home page at [www.gao.gov](http://www.gao.gov).

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<sup>1</sup>Pub. L. No. 111-5, 123 Stat. 115 (February 17, 2009).

<sup>2</sup>GAO-09-453T.

<sup>3</sup>Recovery Act, div. A, title IX, §901

<sup>4</sup>GAO-09-580.

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Like the report, my statement this morning discusses (1) selected states' and localities' uses of and planning for Recovery Act funds, (2) the approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of the Recovery Act funds they received. Our report addresses each of these objectives in detail and contains an appendix on each of the 16 states and the District of Columbia (the District) where we did our detailed work that discusses our reporting objectives as they apply to each of those locations.

As discussed in my March testimony, we selected a core group of 16 states and the District that we will follow over the next few years to provide an ongoing longitudinal analysis of the use of funds provided in conjunction with the Recovery Act. The states are Arizona, California, Colorado, Florida, Georgia, Iowa, Illinois, Massachusetts, Michigan, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas. These states contain about 65 percent of the U.S. population and are estimated to receive collectively about two-thirds of the intergovernmental federal assistance funds available through the Recovery Act. We selected these states and the District on the basis of outlay projections, percentage of the U.S. population represented, unemployment rates and changes, and a mix of states' poverty levels, geographic coverage, and representation of both urban and rural areas. In addition for this bimonthly review, we visited a non-probability sample of about 60 localities within the 16 selected states.<sup>3</sup>

We collected documents from and conducted semi-structured interviews with executive-level state and local officials and staff from Governors' offices, "Recovery Czars," State Auditors, Controllers, and Treasurers. We also interviewed staff from state legislatures. In addition, our work focused on federal, state, and local agencies administering programs receiving Recovery Act funds. We analyzed data and interviewed officials from the federal Office of Management and Budget (OMB). We also analyzed other federal guidance on programs selected for this review and spoke with relevant program officials at the Centers for Medicare & Medicaid Services (CMS), the U.S. Department of Transportation and the U.S. Department of Education. We did not review state legal materials for this report, but relied on state officials and other state sources for description and interpretation of relevant state constitutions, statutes,

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<sup>3</sup>This total includes two entities in the District which received direct federal funding that was not passed through the District government.

legislative proposals, and other state legal materials. A detailed description of our scope and methodology can be found in an appendix to our report.

We conducted a performance audit for our first bimonthly review from February 17, 2009, to April 20, 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

In addition to our ongoing work on selected states' and localities' use of Recovery Act funding, we have completed two of the other mandates included for us in the Recovery Act. First, on April 3, 2009, we announced the appointment of 13 members to the Health Information Technology Policy Committee, a new advisory body established by the Recovery Act. Additionally, on April 16, 2009, we issued a report on the actions of the Small Business Administration (SBA) to, among other things, increase liquidity in the secondary market for SBA loans.<sup>6</sup>

## Summary of GAO Findings

### Uses of Funds

About 90 percent of the estimated \$49 billion Recovery Act funding to be provided to states and localities in fiscal year 2009 will be through health, transportation and education programs. Within these categories, the three largest programs are increased Medicaid Federal Medical Assistance Percentage (FMAP) grant awards, funds for highway infrastructure investment, and the State Fiscal Stabilization Fund (SFSF). Table 1 shows the breakout of funding available for these three programs in the 16 selected states and the District. The Recovery Act funding for these 17 jurisdictions accounts for a little less than two-thirds of total Recovery Act funding for these three programs.

<sup>6</sup> GAO, *Small Business Administration's Implementation of Administrative Provisions in the American Recovery and Reinvestment Act of 2009*, GAO-09-507R (Washington, D.C.: April 16, 2009).

**Table 1: Notification of Recovery Act Funds for GAO Core States and the District for Select Programs (Dollars in thousands)**

State	Medicaid FMAP	Highways	Fiscal Stabilization Fund
Arizona	\$534,576	\$521,958	\$681,360
California	\$3,331,167	\$2,569,568	\$3,993,379
Colorado	\$226,959	\$403,924	\$509,363
District of Columbia	\$87,831	\$123,508	\$59,883
Florida	\$1,394,945	\$1,346,735	\$1,809,196
Georgia	\$521,251	\$931,586	\$1,032,684
Illinois	\$992,042	\$935,593	\$1,376,965
Iowa	\$136,023	\$358,162	\$316,467
Massachusetts	\$1,182,968	\$437,865	\$666,153
Michigan	\$700,522	\$847,205	\$1,066,733
Mississippi	\$225,471	\$354,564	\$321,131
New Jersey	\$549,847	\$651,774	\$891,424
New York	\$3,143,641	\$1,120,685	\$2,021,924
North Carolina	\$657,111	\$735,527	\$951,704
Ohio	\$760,647	\$935,677	\$1,198,882
Pennsylvania	\$1,043,920	\$1,026,429	\$1,276,766
Texas	\$1,448,824	\$2,250,015	\$2,662,203
Total Case Study	\$16,937,745	\$15,550,776	\$20,836,218
Percent of National Total	70	58	64
<b>National Total</b>	<b>\$24,233,145</b>	<b>\$26,660,000</b>	<b>\$32,552,620</b>
<b>Notifications as of</b>	<b>April 3, 2009</b>	<b>March 2, 2009</b>	<b>April 2, 2009</b>

Source: GAO analysis of agency data.

Note: For Medicaid FMAP amounts shown are the increased Medicaid FMAP Grant Awards as of April 3, 2009. For Highways, the amounts shown are the full state apportionment. For the SFSF, the amounts shown are the initial release of the state allocation.

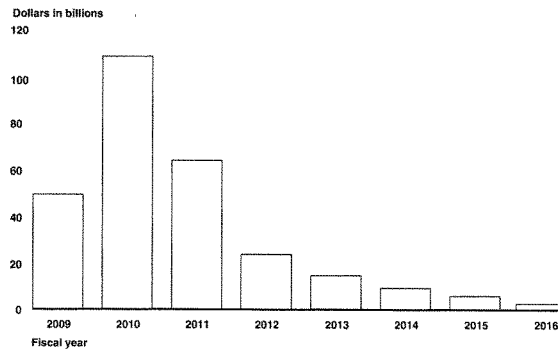
#### Increased Medicaid FMAP Funding

The 16 states and the District have drawn down approximately \$7.96 billion in increased FMAP grant awards for the period October 1, 2008, through April 1, 2009. The increased FMAP is for state expenditures for Medicaid services. The receipt of this increased FMAP may reduce the state share for their Medicaid programs. States have reported using funds made available as a result of the increased FMAP for a variety of purposes. For example, states and the District most frequently reported using these funds to maintain their current level of Medicaid eligibility and benefits, cover their increased Medicaid caseloads—which are primarily populations that are sensitive to economic downturns, including children and families,

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	and to offset their state general fund deficits, thereby avoiding layoffs and other measures detrimental to economic recovery.
Highway Infrastructure Investment	States are undertaking planning activities to identify projects, obtain approval at the state and federal level, and move them to contracting and implementation. Some state officials told us they were focusing on construction and maintenance projects, such as road and bridge repairs. Before they can expend Recovery Act funds, states must reach agreement with the Department of Transportation on the specific projects; as of April 16, 2009, two of the 16 states had agreements covering more than 50 percent of their states' apportioned funds, and three states did not have agreement on any projects. While a few, including Mississippi and Iowa had already executed contracts, most of the 16 states were planning to solicit bids in April or May. Thus, states generally had not yet expended significant amounts of Recovery Act funds.
State Fiscal Stabilization Fund	<p>The states and the District must apply to the Department of Education for SFSF funds. Education will award funds once it determines that an application contains key assurances and information on how the state will use the funds. As of April 20, applications from three states had met that determination—South Dakota, and two of GAO's sample states, California and Illinois. The applications from other states are being developed and submitted and have not yet been awarded. The states and the District report that SFSF funds will be used to hire and retain teachers, reduce the potential for layoffs, cover budget shortfalls, and restore funding cuts to programs.</p> <p>Planning continues for the use of Recovery Act funds. Figure 1 below shows the projected timing when funds will be made available to states and localities.</p>

**Figure 1: Projected Timing of Federal Recovery Act Funding Made Available to States and Localities by Fiscal Year**



Source: GAO analysis of CBO and FFIS data.

State planning activities include appointing Recovery Czars, establishing task forces and other entities, and developing public websites to solicit input and publicize selected projects. In many states, legislative authorization is needed before the state can receive and/or expend funds or make changes to programs or eligibility requirements.

#### Accountability Approaches

We found that the selected states and the District are taking various approaches to ensure that internal controls are in place to manage risk up-front; they are assessing known risks and developing plans to address those risks. However, officials in most of the states and the District expressed concerns regarding the lack of Recovery Act funding provided for accountability and oversight. Due to fiscal constraints, many states reported significant declines in the number of oversight staff—limiting their ability to ensure proper implementation and management of Recovery Act funds. State auditors are also planning their work including conducting required single audits and testing compliance with federal requirements. The single audit process is important for effective oversight but can be modified to be a more timely and effective audit and oversight



	<p>tool for the Recovery Act and OMB is weighing options on how to modify it.</p> <p>Nearly half of the estimated spending programs in the Recovery Act will be administered by non-federal entities. State officials suggested opportunities to improve communication in several areas. For example, they wish to be notified when Recovery Act funds are made available directly to prime recipients within their state that are not state agencies.</p>
Plans to Evaluate Impact	An important objective of the Recovery Act is to preserve and create jobs and promote economic recovery. Officials in nine of the 16 states and the District expressed concern about determining jobs created and retained under the Recovery Act, as well as methodologies that can be used for estimation of each.
GAO's Recommendations	OMB has moved out quickly to guide implementation of the Recovery Act. As OMB's initiatives move forward, it has opportunities to build upon its efforts to date by addressing several important issues.
Accountability and Transparency Requirements	<p>The Director of OMB should:</p> <ul style="list-style-type: none"> <li>• adjust the single audit process to provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010.</li> <li>• continue efforts to identify methodologies that can be used to determine jobs created and retained from projects funded by the Recovery Act.</li> <li>• evaluate current requirements to determine whether sufficient, reliable and timely information is being collected before adding further data collection requirements.</li> </ul>
Administrative Support and Oversight	The Director of OMB should clarify what Recovery Act funds can be used to support state efforts to ensure accountability and oversight.
Communications	The Director of OMB should provide timely and efficient notification to (1) prime recipients in states and localities when funds are made available for their use, (2) states, where the state is not the primary recipient of funds, but has a state-wide interest in this information, and (3) all recipients, on

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planned releases of federal agency guidance and whether additional guidance or modifications are expected.

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### OMB, States, and District Comments on the Draft of Our Report

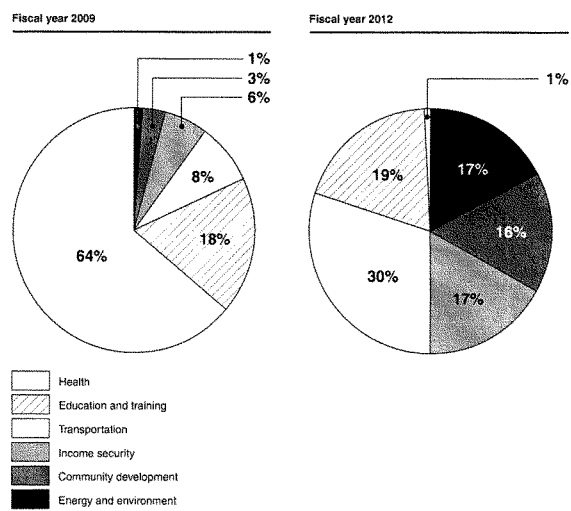
We provided the Director of the Office of Management and Budget with a draft of this report for comment on April 20, 2009. OMB staff responded the next day, noting that in its initial review, OMB concurred with the overall objectives of our recommendations. OMB staff also provided some clarifying information, adding that OMB will complete a more thorough review in a few days. We have incorporated OMB's clarifying information as appropriate. In addition, OMB said it plans to work with us to define the best path forward on our recommendations and to further the accountability and transparency of the Recovery Act. The Governors of each of the 16 states and the Mayor of the District were provided drafts for comment on each of their respective appendixes in this report. Those comments are included in the appendixes.

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### Background

Over time, the programmatic focus of Recovery Act spending will change. As shown in figure 2, about two-thirds of Recovery Act funds expected to be spent by states in the current 2009 fiscal year will be health-related spending, primarily temporary increases in Medicaid FMAP funding. Health, education, and transportation is estimated to account for approximately 90 percent of fiscal year 2009 Recovery Act funding for states and localities. However, by fiscal year 2012, transportation will be the largest share of state and local Recovery Act funding. Taken together, transportation spending, along with investments in community development, energy, and environmental areas that are geared more toward creating long-run economic growth opportunities, will represent approximately two-thirds of state and local Recovery Act funding in 2012.

**Figure 2: Composition of State and Local Recovery Act Funding, Fiscal Years 2009 and 2012**



Source: GAO analysis of CBO and FFIS data.

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**States' and Localities'  
Use of and Plans for  
Recovery Act Funds  
Focuses on Purposes  
of the Act and States'  
Fiscal Stresses**

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**Medicaid FMAP**

Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income.<sup>7</sup> The amount of federal assistance states receive for Medicaid service expenditures is known as the FMAP.

Under the Recovery Act, states are eligible for an increased FMAP for expenditures that states make in providing services to their Medicaid populations.<sup>8</sup> The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008 and December 31, 2010. On February 25, 2009, CMS made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>9</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for: (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. For the first two quarters of 2009, the increases in

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<sup>7</sup>States may use certain sources for financing the non-federal share of Medicaid expenditures, including contributions from political subdivisions in the state, such as cities or counties.

<sup>8</sup>See Recovery Act, div. B, title V, § 5001 (a)-(c). U.S. territories are also eligible for an increased FMAP subject to a different formula than states. Recovery Act div. B, title V, § 5001 (d).

<sup>9</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for Medicaid service expenditures made on or after October 1, 2008.

the FMAP for the 16 states and the District ranged from 7.09 percentage points in Iowa to 11.59 percentage points in California, as shown in table 2.

**Table 2: FMAP Changes from Fiscal Year 2008 to the First Two Quarters of Fiscal Year 2009, for 16 states and the District**

State	FY 2008 FMAP	FY 2009 FMAP, first two quarters	Difference
Arizona	66.20	75.01	8.81
California	50.00	61.59	11.59
Colorado	50.00	58.78	8.78
District of Columbia	70.00	77.68	7.68
Florida	56.83	67.64	10.81
Georgia	63.10	73.44	10.34
Illinois	50.00	60.48	10.48
Iowa	61.73	68.82	7.09
Massachusetts	50.00	58.78	8.78
Michigan	58.10	69.58	11.48
Mississippi	76.29	83.62	7.33
New Jersey	50.00	58.78	8.78
New York	50.00	58.78	8.78
North Carolina	64.05	73.55	9.50
Ohio	60.79	70.25	9.46
Pennsylvania	54.08	63.05	8.97
Texas	60.56	68.76	8.20

Source: GAO analysis of HHS data.

In our sample of 16 states and the District, officials from 15 states and the District indicated that they had drawn down increased FMAP grant awards, totaling \$7.96 billion for the period of October 1, 2008 through April 1, 2009—47 percent of their increased FMAP grant awards. In our sample, the extent to which individual states and the District accessed these funds varied widely, ranging from 0 percent in Colorado to about 66 percent in New Jersey. Nationally, the 50 states and several territories combined have drawn down approximately \$11 billion as of April 1, 2009,

which represents almost 46 percent of the increased FMAP grants awarded for the first three quarters of federal fiscal year 2009 (table 3).<sup>10</sup>

**Table 3: FMAP Grant Awards and Funds Drawn Down, for 16 States and the District**

(Dollars in thousands)

State	FMAP grant awards	Funds drawn	Percentage of funds drawn
Arizona	\$534,576	\$286,286	53.6
California	\$3,331,167	\$1,511,539	45.4
Colorado	\$226,959	0	0.0
District of Columbia	\$87,831	\$49,898	56.8
Florida	\$1,394,945	\$817,025	58.6
Georgia	\$521,251	\$311,515	59.8
Illinois	\$992,042	\$117,081	11.8
Iowa	\$136,023	\$81,663	60.0
Massachusetts	\$1,182,968	\$272,559	23.0
Michigan	\$700,522	\$462,982	66.1
Mississippi	\$225,471	\$114,112	50.6
New Jersey	\$ 549,847	\$362,235	65.9
New York	\$3,143,641	\$1,739,073	55.3
North Carolina	\$657,111	\$414,644	63.1
Ohio	\$760,647	\$420,630	55.3
Pennsylvania	\$1,043,920	\$330,811	31.7
Texas	\$1,448,824	\$665,665	45.9
<b>Total</b>	<b>\$16,937,745</b>	<b>\$7,957,718</b>	<b>47.0</b>

Source: GAO analysis of HHS data.

Note: FMAP grant awards are those funds awarded as of April 3, 2009, and funds drawn down are as of April 1, 2009.

In order for states to qualify for the increased FMAP available under the Recovery Act, they must meet certain requirements. In particular

- **Maintenance of Eligibility:** In order to qualify for the increased FMAP, states generally may not apply eligibility standards, methodologies, or procedures that are more restrictive than those in

<sup>10</sup>This amount includes funds drawn down by U.S. territories and the District.

effect under their state Medicaid programs on July 1, 2008.<sup>11</sup> In guidance to states, CMS noted that examples of restrictions of eligibility could include (1) the elimination of any eligibility groups since July 1, 2008 or (2) changes in an eligibility determination or redetermination process that is more stringent than what was in effect on July 1, 2008. States that fail to initially satisfy the maintenance of eligibility requirements have an opportunity to reinstate their eligibility standards, methodologies, and procedures before July 1, 2009 and become retroactively eligible for the increased FMAP.

- **Compliance with Prompt Payment:** Under federal law states are required to pay claims from health practitioners promptly.<sup>12</sup> Under the Recovery Act, states are prohibited from receiving the increased FMAP for days during any period in which that state has failed to meet this requirement.<sup>13</sup> Although the increased FMAP is not available for any claims received from a practitioner on each day the state is not in compliance with these prompt payment requirements, the state may receive the regular FMAP for practitioner claims received on days of non-compliance. CMS officials told us that states must attest that they are in compliance with the prompt payment requirement, but that enforcement is complicated due to differences across states in methods used to track this information. CMS officials plan to issue guidance on reporting compliance with the prompt payment requirement and are currently gathering information from states on the methods they use to determine compliance.
- **Rainy Day Funds:** States are not eligible for an increased FMAP if any amounts attributable (either directly or indirectly) to the increased FMAP are deposited or credited into any reserve or rainy day fund of the state.<sup>14</sup>
- **Percentage Contributions from Political Subdivisions:** In some states, political subdivisions—such as cities and counties—may be

<sup>11</sup>See Recovery Act § 5001(f)(1).

<sup>12</sup>States are required to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt. See 42 U.S.C. § 1396a(a)(37)(A).

<sup>13</sup>This provision only applies to claims received after February 17, 2009, the date of enactment of the Recovery Act. See Recovery Act § 5001(f)(2).

<sup>14</sup>This prohibition does not apply to any increase in FMAP based on maintenance of the states' prior year FMAPs.

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required to help finance the state's share of Medicaid spending. States that have such financing arrangements are not eligible to receive the increased FMAP if the percentage contributions required to be made by a political subdivision are greater than what was in place on September 30, 2008.<sup>15</sup>

In addition to meeting the above requirements, states that receive the increased FMAP must submit a report to CMS no later than September 30, 2011 that describes how the increased FMAP funds were expended, in a form and manner determined by CMS.<sup>16</sup> In guidance to states, CMS has stated that further guidance will be developed for this reporting requirement. CMS guidance to states also indicates that, for federal reimbursement, increased FMAP funds must be drawn down separately, tracked separately, and reported to CMS separately. Officials from several states told us they require additional guidance from CMS on tracking receipt of increased FMAP funds and on reporting on the use of these funds.

The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services.<sup>17</sup> However, the receipt of this increased FMAP may reduce the state share for their Medicaid programs. States have reported using these available funds for a variety of purposes. In our sample, individual states and the District reported that they would use the funds to maintain their current level of Medicaid eligibility and benefits, cover their increased Medicaid caseloads—which are primarily populations that are sensitive to economic downturns, including children and families, and to offset their state general fund deficits thereby avoiding layoffs and other measures detrimental to economic recovery. Ten states and the District reported using these funds to maintain program eligibility. Nine states and the District reported using these funds to maintain benefits. Specifically, Massachusetts reported that during a previous financial downturn, the state limited the number of individuals eligible for some services and reduced certain program benefits that were optional for the state to cover. However, with the funds made available as a result of the increased FMAP, the state did not have to make such reductions.

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<sup>15</sup>This prohibition does not apply to any increase in FMAP based on maintenance of the states' prior year FMAPs.

<sup>16</sup>Recovery Act, div. B, title V, § 5001 (g)(1).

<sup>17</sup>Recovery Act, div. B, title V, § 5001 (a)-(c), (h)(1).



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Similarly, New Jersey reported that the state used these funds to eliminate premiums for certain children in its State Children's Health Insurance Program, allowing it to retain coverage for children whose enrollment in the program would otherwise have been terminated for non-payment of premiums.

Nine states and the District reported using these funds to cover increases to their Medicaid caseloads, primarily to populations that are sensitive to economic downturns, such as children and families. For example, New Jersey indicated that these funds would help the state meet the increased demand for Medicaid services. According to a New Jersey official, due to significant job losses, the state's proposed 2010 budget would not have accommodated all the applicants newly eligible for Medicaid and that the funds available as a result of the increased FMAP have allowed the state to maintain a "safety net" of coverage for uninsured and unemployed people. Six states in our sample also reported that they used funds made available as a result of the increased FMAP to comply with prompt payment requirements. Specifically, Illinois reported that these funds will permit the state to move from a 90-day payment cycle to a 30-day payment cycle for all Medicaid providers. Three states also reported using these funds to restore or to increase provider payment rates.

In addition, 10 states and the District indicated that the funds made available as a result of the increased FMAP would help offset deficits in their general funds. Pennsylvania reported that because funding for its Medicaid program is derived, in part, from state revenues, program funding levels fluctuate as the economy rises and falls. However, the state was able to use the funds made available to offset the effects of lower state revenues. Arizona officials also reported that the state used funds made available as a result of the increased FMAP to pay down some of its debt and make payroll payments, thus allowing the state to avoid a serious cash flow problem.

In our sample, many states and the District indicated that they need additional guidance from CMS regarding eligibility for the increased FMAP funds. Specifically, 5 states raised concerns about whether certain programmatic changes could jeopardize the state's eligibility for these funds. For example, Texas officials indicated that guidance from CMS is needed regarding whether certain programmatic changes being considered by Texas, such as a possible extension of the program's eligibility period, would affect the state's eligibility for increased FMAP funds. Similarly, Massachusetts wanted clarification from CMS as to whether certain changes in the timeframe for the state to conduct eligibility re-

determinations would be considered a more restrictive standard. Four states also reported that they wanted additional guidance from CMS regarding policies related to the prompt payment requirements or changes to the non-federal share of Medicaid expenditures. For example, California officials noted that the state reduced Medicaid payments for in-home support services, but that counties could voluntarily choose to increase these payments without altering the cost sharing arrangements between the counties and the state. The state wants clarification from CMS on whether such an arrangement would be allowable in light of the Recovery Act requirements regarding the percentage of contributions by political subdivisions within a state toward the non-federal share of expenditures.

In response to states' concerns regarding the need for guidance, CMS told us that it is in the process of developing draft guidance on the prompt payment provisions in the Recovery Act. One official noted that this guidance will include defining the term practitioner, describing the types of claims applicable under the provision, and addressing the principles that are integral to determining a state's compliance with prompt payment requirements. Additionally, CMS plans to have a reporting mechanism in place through which states would report compliance under this provision. With regard to Recovery Act requirements regarding political subdivisions, CMS described their current activities for providing guidance to states. Due to the variability of state operations, funding processes, and political structures, CMS has been working with states on a case-by-case basis to discuss particular issues associated with this provision and to address the particular circumstances for each state. A CMS official told us that if there were an issue(s) or circumstance(s) that had applicability across the states, or if there were broader themes having national significance, CMS would consider issuing guidance.

#### Highway Infrastructure Investment

The Recovery Act provides approximately \$48 billion to fund grants to states, localities and regional authorities for transportation projects of which the largest piece is \$27.5 billion for highway and related infrastructure investments. The Recovery Act largely provides for increased transportation funding through existing programs such as the Federal-Aid Highway Surface Transportation Program—a federally funded, state-administered program. Under this program, funds are apportioned annually to each state department of transportation (or equivalent) to construct and maintain roadways and bridges on the federal-aid highway system. The Federal-Aid Highway Program refers to the separately funded formula grant programs administered by the Federal Highway Administration (FHWA) in the U.S. Department of Transportation.

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Of the \$27.5 billion provided in the Recovery Act for highway and related infrastructure investments, \$26.7 billion is provided to the 50 states for restoration, repair, construction and other activities allowed under the Federal-Aid Highway Surface Transportation Program. Nearly one-third of these funds are required to be sub-allocated to metropolitan and other areas. States must follow the requirements for the existing program, and in addition, the Recovery Act requires that the Governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. The certifications must include a statement of the amount of funds the state planned to expend from state sources as of the date of enactment, during the period beginning on the date of enactment through September 30, 2010, for the types of projects that are funded by the appropriation.

The U.S. Department of Transportation is reviewing the Governors' certifications regarding maintaining their level of effort for highways. According to the Department, of the 16 states in our review and the District, three states have submitted a certification free of explanatory or conditional language—Arizona, Michigan, and New York. Eight submitted “explanatory” certifications—certifications that used language that articulated assumptions used or stated the certification was based on the “best information available at the time,” but did not clearly qualify the expected maintenance of effort on the assumptions proving true or information not changing in the future. Six submitted a “conditional” certification, which means that the certification was subject to conditions or assumptions, future legislative action, future revenues, or other conditions.<sup>18</sup>

Recovery Act funding for highway infrastructure investment differs from the usual practice in the Federal-Aid Highway Program in a few important ways. Most significantly, for projects funded under the Recovery Act, the federal share is 100 percent; typically projects require a state match of 20 percent while the federal share is typically 80 percent. Under the Recovery Act, priority is also to be given to projects that are projected to be completed within three years. In addition, within 120 days after the

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<sup>18</sup>The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

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apportionment by the Department of Transportation to the states (March 2, 2009), 50 percent of the apportioned funds must be obligated.<sup>18</sup> Any amount of this 50 percent of apportioned funding that is not obligated may be withdrawn by the Secretary of Transportation and redistributed to other states that have obligated their funds in a timely manner. Furthermore, one year after enactment, the Secretary will withdraw any remaining unobligated funds and redistribute them based on states' need and ability to obligate additional funds. These provisions are applicable only to those funds apportioned to the state and not those funds required by the Recovery Act to be suballocated to metropolitan, regional and local organizations.

Finally, states are required to give priority to projects that are located in economically distressed areas as defined by the Public Works and Economic Development Act of 1965, as amended. In March 2009, FHWA directed its field offices to provide oversight and take appropriate action to ensure that states gave adequate consideration to economically distressed areas in selecting projects. Specifically, field offices were directed to discuss this issue with the states and to document its review and oversight of this process.

States are undertaking planning activities to identify projects, obtain approval at the state and federal level, and move projects to contracting and implementation. However, because of the steps necessary before implementation, states generally had not yet expended significant amounts of Recovery Act Funds. States are required to reach agreement with DOT on a list of projects. States will then request reimbursement from DOT as the state makes payments to contractors working on approved projects.

As of April 16, 2009, the U.S. Department of Transportation reported that nationally \$6.4 billion of the \$26.6 billion in Recovery Act highway infrastructure investment funding provided to the states had been obligated—meaning Transportation and the states had reached agreements on projects worth this amount. As shown in Table 4 below, for the locations that GAO reviewed, the extent to which the Department of Transportation had obligated funds apportioned to the states and the

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<sup>18</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

District ranged from 0 to 65 percent. For two of the states, the Department of Transportation had obligated over 50 percent of the states' apportioned funds, for 4 it had obligated 30 to 50 percent of the states' funds, for 9 states it had obligated under 30 percent of funds, and for three it had not obligated any funds.

**Table 4: Highway Apportionments and Obligations as of April 16, 2009 (Dollars in millions)**

State	Amount apportioned	Amount obligated	Percent of apportionment obligated	Number of projects
Arizona	\$522	\$148	28	26
California	2,570	261	10	20
Colorado	404	118	29	19
District of Columbia	124	37	30	1
Florida	1,347	0	0	0
Georgia	932	0	0	0
Illinois	936	606	65	214
Iowa	358	221	62	107
Massachusetts	425	64	15	19
Michigan	847	111	13	27
Mississippi	355	137	39	32
New Jersey	652	281	43	12
New York	1,121	277	25	108
North Carolina	736	165	22	53
Ohio	936	0	0	0
Pennsylvania	1,026	309	30	108
Texas	2,250	534	24	159
<b>Total</b>	<b>\$15,538</b>	<b>\$3,269</b>	<b>21</b>	<b>905</b>

Source: FHWA.

Note: Totals may not add due to rounding.

While most states we visited had not yet expended significant funds, some told us they were planning to solicit bids in April or May. Officials, also stated that they planned to meet statutory deadlines for obligating the highway funds. A few states had already executed contracts. As of April 1, 2009, the Mississippi Department of Transportation (MDOT), for example,

had signed contracts for 10 projects totaling approximately \$77 million.<sup>20</sup> These projects include the expansion of State Route 19 in eastern Mississippi into a four-lane highway. This project fulfills part of MDOT's 1987 Four-Lane Highway Program which seeks to link every Mississippian to a four-lane highway within 30 miles or 30 minutes. Similarly, as of April 15, 2009, the Iowa Department of Transportation had competitively awarded 25 contracts valued at \$168 million. Most often however, we found that highway funds in the states and the District have not yet been spent because highway projects were at earlier stages of planning, approval, and competitive contracting. For example, in Florida, the Department of Transportation (FDOT) plans to use the Recovery Act funds to accelerate road construction programs in its preexisting 5-year plan which will result in some projects being reprioritized and selected for earlier completion. On April 15, 2009, the Florida Legislative Budget Commission approved the Recovery Act-funded projects that FDOT had submitted.

For the most part, states were focusing their selection of Recovery Act-funded highway projects on construction and maintenance, rather than planning and design, because they were seeking projects that would have employment impacts and could be implemented quickly. These included road repairs and resurfacing, bridge repairs and maintenance, safety improvements, and road widening. For example, in Illinois, the Department of Transportation is planning to spend a large share of its estimated \$655 million in Recovery Act funds<sup>21</sup> for highway and bridge construction and maintenance projects in economically distressed areas, those that are shovel-ready, and those that can be completed by February 2012. In Iowa, the contracts awarded have been for projects such as bridge replacements and highway resurfacing—shovel-ready projects that could be initiated and completed quickly. Knowing that the Recovery Act would include opportunities for highway investment, states told us they worked

<sup>20</sup> As of April 16, 2009, the U.S. Department of Transportation had obligated \$137.0 million for 32 Mississippi projects.

<sup>21</sup> According to the Federal Highway Administration, Illinois' share of Recovery Act funds for highway infrastructure investment is approximately \$936 million. This total consists of \$655 million for IDOT projects and \$281 million in sub-allocations for local governments' highway projects. The \$655 million to IDOT includes \$627 million for IDOT to use statewide and \$28 million for mandatory transportation enhancements. Transportation enhancements include activities such as provision of facilities for pedestrians and bicyclists, preservation of abandoned railway corridors, acquisition of scenic easements, and historic preservation projects.

in advance of the legislation to identify appropriate projects. For example, in New York, the state DOT began planning to manage anticipated federal stimulus money in November 2008. A key part of New York's DOT's strategy was to build on existing planning and program systems to distribute and manage the funds.

#### State Fiscal Stabilization Fund

The Recovery Act provided \$53.6 billion in appropriations for the State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education. The Act requires that the Secretary set aside \$5 billion for State Incentive Grants, referred to by the department as the Reach for the Top program, and the establishment of an Innovation Fund. The Recovery Act specifies that 81.8 percent (about \$39.5 billion) is to be distributed to states for support of elementary, secondary, and postsecondary education, and early childhood education programs. The remaining 18.2 percent of SFSF (about \$8.8 billion) is available for basic government services but may also be used for educational purposes. These funds are to be distributed to states by formula, with 61 percent of the state award based on the state's relative share of the population aged 5 to 24 and 39 percent based on the state's relative share of the total U.S. population. The Department of Education announced on April 1, 2009 that it will award the SFSF in two phases. The first phase—\$32.6 billion—represents about two-thirds of the SFSF.

The states and the District must apply to the Department of Education for SFSF funds and Education must approve those applications. As of April 20, 2009, applications from three states had been approved—South Dakota, and two of GAO's sample states, California and Illinois. Since applications from other states are now being developed and submitted, they have not yet received their SFSF funds. The applications to Education must contain certain assurances. For example, states must assure that, in each of fiscal years 2009, 2010, and 2011, they will maintain state support at fiscal year 2006 levels for elementary and secondary education and also for public institutions of higher education (IHEs). However, the Secretary of Education may waive maintenance of effort requirements if the state demonstrates that it will commit an equal or greater percentage of state revenues to education than in the previous applicable year. The state application must also contain (1) assurances that the state is committed to advancing education reform in increasing teacher effectiveness, establishing state-wide education longitudinal data systems, and improving the quality of state academic standards and assessments; (2) baseline data that demonstrates the state's current status in each of the education reform areas; and (3) a description of how the state intends to use its stabilization allocation.

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Within two weeks of receipt of an approvable SFSF application, Education will provide the state with 67 percent of its SFSF allocation. Under certain circumstances, Education will provide the state with up to 90 percent of its allocation. In the second phase, Education intends to conduct a full peer review of state applications before awarding the final allocations.

After maintaining state support for education at fiscal year 2006 levels, states are required to use the education portion of the SFSF to restore state support to the greater of fiscal year 2008 or 2009 levels for elementary and secondary education, public IHEs, and, if applicable, early childhood education programs. States must distribute these funds to school districts using the primary state education formula but maintain discretion in how funds are allocated to public IHEs. If, after restoring state support for education, additional funds remain, the state must allocate those funds to school districts according to the Title I, Part A funding formula. However, if a state's education stabilization fund allocation is insufficient to restore state support for education, then a state must allocate funds in proportion to the relative shortfall in state support to public schools and IHEs. Education stabilization funds must be allocated to school districts and public IHEs and cannot be retained at the state level.

Once stabilization funds are awarded to school districts and public IHEs, they have considerable flexibility over how they use those funds. School districts are allowed to use stabilization funds for any allowable purpose under the Elementary and Secondary Education Act (ESEA), (commonly known as the No Child Left Behind Act), the Individuals with Disabilities Education Act (IDEA), the Adult Education and Family Literacy Act, or the Perkins Act, subject to some prohibitions on using funds for, among other things, sports facilities and vehicles. In particular, because allowable uses under the Impact Aid provisions of ESEA are broad, school districts have discretion to use Recovery Act funding for things ranging from salaries of teachers, administrators, and support staff to purchases of textbooks, computers, and other equipment. The Recovery Act allows public IHEs to use SFSF funds in such a way as to mitigate the need to raise tuition and fees, as well as for the modernization, renovation, and repair of facilities, subject to certain limitations. However, the Recovery Act prohibits public IHEs from using stabilization funds for such things as increasing endowments, modernizing, renovating, or repairing sports facilities, or maintaining equipment. According to Education officials, there are no maintenance of effort requirements placed on local school districts. Consequently, as long as local districts use stabilization funds for



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allowable purposes, they are free to reduce spending on education from local-source funds, such as property tax revenues.

States have broad discretion over how the \$8.8 billion in SFSF funds designated for basic government services are used. The Recovery Act provides that these funds can be used for public safety and other government services and that these services may include assistance for education, as well as for modernization, renovation, and repairs of public schools or IHEs, subject to certain requirements. Education's guidance provides that the funds can also be used to cover state administrative expenses related to the Recovery Act. However, the Act also places several restrictions on the use of these funds. For example, these funds cannot be used to pay for casinos (a general prohibition that applies to all Recovery Act funds), financial assistance for students to attend private schools, or construction, modernization, renovation, or repair of stadiums or other sports facilities.

States expected that SFSF uses by school districts and public IHEs would include retaining current staff and spending on programmatic initiatives, among other uses. Some states' fiscal condition could affect their ability to meet maintenance of effort (MOE) requirements in order to receive SFSF monies, but they are awaiting final guidance from Education on procedures to obtain relief from these requirements. For example, due to substantial revenue shortages, Florida has cut its state budget in recent years and the state will not be able to meet the maintenance-of-effort requirement to readily qualify for these funds. The state will apply to Education for a waiver from this requirement; however, it is awaiting final instructions from Education on submission of the waiver. Florida plans to use SFSF funds to reduce the impact of any further cuts that may be needed in the state education budget.

In Arizona, state officials expect that SFSF recipients, such as local school districts, will generally use their allocations to improve the tools they use to assess student performance and determine to what extent performance meets federal academic standards, rehire teachers that were let go because of prior budget cuts, retain teachers, and meet the federal requirement that all schools have equal access to highly qualified teachers, among other things. Funds for the state universities will help them maintain services and staff as well as avoid tuition increases. Illinois officials stated that the state plans to use all of the \$2 billion in State Fiscal Stabilization funds, including the 18.2 percent allowed for government services, for K-12 and higher education activities and hopes to avert layoffs and other cutbacks many districts and public colleges and universities are

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Plans to Track Recovery Act Funds

facing in their fiscal year 2009 and 2010 budgets. State Board of Education officials also noted that U.S. Department of Education guidance allows school districts to use stabilization funds for education reforms, such as prolonging school days and school years, where possible. However, officials said that Illinois districts will focus these funds on filling budget gaps rather than implementing projects that will require long-term resource commitments. While planning is underway, most of the selected states reported that they have not yet fully decided how to use the 18.2 percent of the SPSF, which is discretionary.

States' and localities' tracking and accounting systems are critical to the proper execution and accurate and timely recording of transactions associated with the Recovery Act. OMB has issued guidance to the states and localities that provides for separate "tagging" of Recovery Act funds so that specific reports can be created and transactions traced. Officials from all 16 of the selected states and the District told us they have established or were establishing methods and processes to separately identify, monitor, track, and report on the use of Recovery Act funds they receive. Officials in some states expressed concern that the use of different accounting software among state agencies may make it difficult to provide consistent and timely reporting. Others reported that their ability to track Recovery Act funds may be affected by state hiring freezes, resulting from budget shortfalls.

State officials reported a range of concerns regarding the federal requirements to identify and track Recovery Act funds going to sub-recipients, localities, and other non-state entities. These concerns include their ability to track these funds within existing systems, uncertainty regarding state officials' accountability for the use of funds which do not pass through state government entities, and their desire for additional federal guidance to establish specific expectations on sub-recipient reporting requirements. Officials in many states expressed concern about being held accountable for funds flowing directly from federal agencies to localities or other recipients. Officials in some states said they would like to at least be informed about funds provided to non-state entities, in order to facilitate planning for their use and so they can coordinate Recovery Act activities.

### States' Actions to Plan for Use of Recovery Act Funds Include New and Existing Entities and Processes

All of the 16 selected states and the District reported taking action to plan for and monitor the use of Recovery Act funding. Some states reported that Recovery Act planning activities for funds received by the state are directed primarily by the governor's office. In New York, for example, the governor provides program direction to the state's departments and offices, and he established a Recovery Act Cabinet comprised of representatives from all state agencies and many state authorities to coordinate and manage Recovery Act funding throughout the state. In North Carolina, Recovery Act planning efforts are led by the newly created Office of Economic Recovery and Investment, which was established by the governor to oversee the state's economic recovery initiatives.

Other states reported that their Recovery Act planning efforts were less centralized. In Mississippi, the governor has little influence over the state Departments of Education and Transportation, as they are led by independent entities. In Texas, oversight of federal Recovery Act funds involves various stakeholders, including the Office of the Governor, the Office of the Comptroller of Public Accounts, and the State Auditor's Office as well as two entities established within the Texas legislature specifically for this purpose—the House Select Committee on Federal Economic Stabilization Funding and the House Appropriations' Subcommittee on Stimulus.<sup>22</sup>

Several states reported that they have appointed "Recovery Czars" or identified a similar key official and established special offices, task forces or other entities to oversee the planning and monitor the use of Recovery Act funds within their states. In Michigan, the governor appointed a Recovery Czar to lead a new Michigan Economic Recovery Office, which is responsible for coordinating Recovery Act programs across all state departments and with external stakeholders such as GAO, the federal OMB, and others.

Some states began planning efforts before Congress enacted the Recovery Act. For example, the state of Georgia recognized the importance of accounting for and monitoring Recovery Act funds and directed state agencies to take a number of steps to safeguard Recovery Act funds and

<sup>22</sup>Under Texas law, the governor is the state's chief budget officer, but the state legislature and the Legislative Budget Board have a large role in the state's budget process, which operates on a 2-year cycle. Both the governor and the Legislative Budget Board develop budget recommendations and submit budget proposals to the legislature, which adopts a budget (general appropriations bill) for the 2-year period.

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mitigate identified risks. Georgia established a small core team in December 2008 to begin planning for the state's implementation of the Recovery Act. Within 1 day of enactment, the governor appointed a Recovery Act Accountability Officer, and she formed a Recovery Act implementation team shortly thereafter. The implementation team includes a senior management team, officials from 31 state agencies, an accountability and transparency support group comprised of officials from the state's budget, accounting, and procurement offices, and five cross-agency implementation teams. At one of the first implementation team meetings, the Recovery Act Accountability Officer disseminated an implementation manual to agencies, which included multiple types of guidance on how to use and account for Recovery Act funds, and new and updated guidance is disseminated at the weekly implementation team meetings.

Officials in other states are using existing mechanisms rather than creating new offices or positions to lead Recovery Act efforts. For example, a District official stated that the District would not appoint a Recovery Czar, and instead would use its existing administrative structures to distribute and monitor Recovery Act funds to ensure quick disbursement of funds. In Mississippi, officials from the Governor's office said that the state did not establish a new office to provide statewide oversight of Recovery Act funding, in part because they did not believe that the Recovery Act provided states with funds for administrative expenses—including additional staff. The Governor did designate a member of his staff to act as a Stimulus Coordinator for Recovery Act activities.

All 16 states we visited and the District have established Recovery Act web sites to provide information on state plans for using Recovery funding, uses of funds to date, and, in some instances, to allow citizens to submit project proposals. For example, Ohio has created [www.recovery.ohio.gov](http://www.recovery.ohio.gov), which represents the state's efforts to create an open, transparent, and equitable process for allocating Recovery Act funds. The state has encouraged citizens to submit proposals for use of Recovery Act funds, and as of April 8, 2009, individuals and organizations from across Ohio submitted more than 23,000 proposals. Iowa officials indicated they want to use the state's recovery web site ([www.recovery.iowa.gov](http://www.recovery.iowa.gov)) to host a "dashboard" function to report updated information on Recovery Act spending that is easily searchable by the public. Also in Colorado, the state plans to create a web-based map of projects receiving recovery funds to help inform the public about the results of Recovery Act spending in Colorado.

### Selected States' and Localities' Internal Controls and Safeguards to Manage and Mitigate the Risk of Mismanagement, Waste, Fraud, and Abuse of Recovery Act Funds

The selected states and the District are taking various approaches to ensure that internal controls are in place to manage risk up-front, rather than after problems develop and deficiencies are identified after the fact, and have different capacities to manage and oversee the use of Recovery Act funds. Many of these differences result from the underlying differences in approaches to governance, organizational structures, and related systems and processes that are unique to each jurisdiction. A robust system of internal control specifically designed to deal with the unique and complex aspects of the Recovery Act funds will be key to helping management of the states and localities achieve the desired results. Effective internal control can be achieved through numerous different approaches, and, in fact, we found significant variation in planned approaches by state. For example,

- New York's Recovery Act cabinet plans to establish a working group on internal controls; the Governor's office plans to hire a consultant to review the state's management infrastructure and capabilities to achieve accountability, effective internal controls, compliance and reliable reporting under the act; and, the state plans to coordinate fraud prevention training sessions.
- Michigan's Recovery Office is developing strategies for effective oversight and tracking of the use of Recovery Act funds to ensure compliance with accountability and transparency requirements.
- Ohio's Office of Internal Audit plans to assess the adequacy and effectiveness of the current internal control framework and test whether state agencies adhere to the framework.
- Florida's Chief Inspector General established an enterprise-wide working group of agency program Inspectors General who are updating their annual work plans by including the Recovery Act funds in their risk assessments and will leave flexibility in their plans to address issues related to funds.
- Massachusetts's Joint Committee on Federal Recovery Act Oversight will hold hearings regarding the oversight of Recovery Act spending.
- Georgia's State Auditor plans to provide internal control training to state agency personnel in late April. The training will discuss basic internal controls, designing and implementing internal controls for Recovery Act programs, best practices in contract monitoring, and reporting on Recovery Act funds.

Internal controls include management and program policies, procedures, and guidance that help ensure effective and efficient use of resources; compliance with laws and regulations; prevention and detection of fraud, waste, and abuse; and the reliability of financial reporting. Because Recovery Act funds are to be distributed as quickly as possible, controls are evolving as various aspects of the program become operational. Effective internal control is a major part of managing any organization to achieve desired outcomes and manage risk. GAO's Standards for Internal Control include five key elements: control environment, risk assessment, control activities, information and communication, and monitoring.<sup>23</sup> Our report contains a discussion of these elements and the related effort underway in the jurisdictions we visited.

#### Current Single Audit Focus May Not Provide Timely Oversight Information for Recovery Act Funds

OMB's Circular No. A-133 sets out implementing guidelines for the single audit and defines roles and responsibilities related to the implementation of the Single Audit Act, including detailed instructions to auditors on how to determine which federal programs are to be audited for compliance with program requirements in a particular year at a given grantee. The Circular No. A-133 Compliance Supplement is issued annually to guide auditors on what program requirements should be tested for programs audited as part of the single audit. OMB has stated that it will use its Circular No. A-133 Compliance Supplement to notify auditors of program requirements that should be tested for Recovery Act programs, and will issue interim updates as necessary.

Both the Single Audit Act and OMB Circular No. A-133 call for a "risk-based" approach to determine which programs will be audited for compliance with program requirements as part of a single audit. In general, the prescribed approach relies heavily on the amount of federal expenditures during a fiscal year and whether findings were reported in the previous period to determine whether detailed compliance testing is required for a given program that year.<sup>24</sup> Under the current approach for risk determination in accordance with Circular No. A-133, certain risks unique to the Recovery Act programs may not receive full consideration.

<sup>23</sup>GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).

<sup>24</sup>The Single Audit Act requires that all major programs be audited and specifies minimum dollar amounts and minimum proportions of federal funds expended for programs to be identified by the auditor as major programs. See 31 U.S.C. §§ 7501.

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Recovery Act funding carries with it some unique challenges. The most significant of these challenges are associated with (1) new government programs, (2) the sudden increase in funds or programs that are new for the recipient entity, and (3) the expectation that some programs and projects will be delivered faster so as to inject funds into the economy. This makes timely and efficient evaluations in response to the Recovery Act's accountability requirements critical. Specifically,

- new programs and recipients participating in a program for the first time may not have the management controls and accounting systems in place to help ensure that funds are distributed and used in accordance with program regulations and objectives;
- Recovery Act funding that applies to programs already in operation may cause total funding to exceed the capacity of management controls and accounting systems that have been effective in past years;
- the more extensive accountability and transparency requirements for Recovery Act funds will require the implementation of new controls and procedures; and
- risk may be increased due to the pressures of spending funds quickly.

In response to the risks associated with Recovery Act funding, the single audit process needs adjustment to put appropriate focus on Recovery Act programs and to provide the necessary level of accountability over these funds in a timely manner. The single audit process could be adjusted to require the auditor to perform procedures such as the following as part of the routine single audit:

- provide for review of the design and implementation of internal control over compliance and financial reporting for programs under the Recovery Act;
- consider risks related to Recovery Act-related programs in determining which federal programs are major programs; and
- specifically, test Recovery Act programs to determine whether the auditee complied with laws and regulations.<sup>25</sup>

The first two items above should preferably be accomplished during 2009 before significant expenditures of funds in 2010 so that the design of internal control can be strengthened prior to the majority of those

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<sup>25</sup>The Single Audit Act sets out minimum federal expenditure amounts and proportions to use as criteria in defining which programs are to be tested for compliance with program requirements during a single audit. OMB will need to consider those statutory criteria when considering revisions to the single audit process.

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expenditures. We further believe that OMB Circular No. A-133 and/or the Circular No. A-133 Compliance Supplement could be adjusted to provide some relief on current audit requirements for low-risk programs to offset additional workload demands associated with Recovery Act funds.

OMB told us that it is developing audit guidance that would address the above audit objectives. OMB also said that it is considering reevaluating potential options for providing relief from certain existing audit requirements in order to provide some balance to the increased requirements for Recovery Act program auditing.

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### State and Local Capacity to Manage Risks

Officials in several states also expressed concerns regarding the lack of funding provided to state oversight entities, given the additional federal requirements placed on states to provide proper accounting and ensure transparency. Due to fiscal constraints, many states reported significant declines in the number of oversight staff, limiting their ability to ensure proper implementation and management of Recovery Act funds. Although the majority of states reported that they lack the necessary resources to ensure adequate oversight of Recovery Act funds, some states reported that they are either hiring new staff or reallocating existing staff for this purpose.

Officials we interviewed in several states said the lack of funding for state oversight entities in the Recovery Act presents them with a challenge, given the increased need for oversight and accountability. According to state officials, state budget and staffing cuts have limited the ability of state and local oversight entities to ensure adequate management and implementation of the Recovery Act. For example, Colorado's state auditor reported that state oversight capacity is limited, noting that the Department of Health Care Policy and Financing has had 3 controllers in the past 4 years and the state legislature's Joint Budget Committee recently cut field audit staff for the Department of Human Services in half. In addition, the Colorado Department of Transportation's deputy controller position is vacant, as is the Department of Personnel & Administration's internal auditor position. Colorado officials noted that these actions are, in part, due to the natural tendency in an economic downturn to cut administrative expenses in an attempt to maintain program delivery levels. Our report contains more examples of capacity issues from our selected states and the District.

Although most states indicated that they lack the resources needed to provide effective monitoring and oversight, some states indicated they will



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hire additional staff to help ensure the prudent use of Recovery Act funds. For example, according to officials with North Carolina's Governor's Crime Commission, the current management capacity in place is not sufficient to implement the Recovery Act. Officials explained that the Recovery Act funds for the Edward Byrne Memorial Justice Assistance Grant program have created such an increase in workload that the department will have to hire additional staff to handle over the next 3 years. Officials explained that these staff will be hired for the short term since the money will run out in 3 years. Additionally, officials explained that they are able to use 10 percent of the Justice Assistance Grants funding to pay for the administrative positions that are needed.

A number of states expressed concerns regarding the ability to track Recovery Act funds due to state hiring freezes, resulting from budget shortfalls. For instance, New Jersey has not increased its number of state auditors or investigators, nor has there been an increase in funding specifically for Recovery Act oversight. In addition, the state hiring freeze has not allowed many state agencies to increase their Recovery Act oversight efforts. For example, despite an increase of \$469 million in Recovery Act funds for state highway projects, no additional staff will be hired to help with those tasks or those directly associated with the Recovery Act, such as reporting on the number of jobs created. While the state's Department of Transportation has committed to shift resources to meet any expanded need for internal Recovery Act oversight, one person is currently responsible for reviewing contractor-reported payroll information for disadvantaged business enterprises, ensuring compliance with Davis-Bacon wage requirements, and development of the job creation figures. State education officials in North Carolina also said that greater oversight capacity is needed to manage the increase in federal funding. However, due to the state's hiring freeze, the agency will be unable to use state funds to hire the additional staff needed to oversee Recovery funds. The North Carolina Recovery Czar said that his office will work with state agencies to authorize hiring additional staff when directly related to Recovery Act oversight.

With respect to oversight of Recovery Act funding at the local level, varying degrees of preparedness were reported by state and local officials. While the California Department of Transportation (Caltrans) officials stated that extensive internal controls exist at the state level, there may be control weaknesses at the local level. Caltrans is collaborating with local entities to identify and address these weaknesses. Likewise, Colorado officials expressed concerns that effective oversight of funds provided to Jefferson County may be limited due to the recent termination of its

internal auditor and the elimination of its internal control audit function. Arizona state officials expressed some concerns about the ability of rural, tribal, and some private entities such as boards, commissions, and nonprofit organizations to manage, especially if the Recovery Act does not provide administrative funding.

### State Plans to Assess Recovery Act Spending Impact

As recipients of Recovery Act funds and as partners with the federal government in achieving Recovery Act goals, states and local units of government are expected to invest Recovery Act funds with a high level of transparency and to be held accountable for results under the Recovery Act. As a means of implementing that goal, guidance has been issued and will continue to be issued to federal agencies, as well as to direct recipients of funding. To date, OMB has issued two broad sets of guidance to the heads of federal departments and agencies for implementing and managing activities enacted under the Recovery Act.<sup>26</sup> OMB has also issued for public comment detailed proposed standard data elements that federal agencies will require from all recipients (except individuals) of Recovery Act funding.<sup>27</sup> When reporting on the use of funds, recipients must show the total amount of recovery funds received from a federal agency, the amount expended or obligated to the project, and project specific information including the name and description of the project, an evaluation of its completion status, the estimated number of jobs created and retained by the project, and information on any subcontracts awarded by the recipient, as specified in the Recovery Act.

State reactions vary widely and often include a mixture of responses to the reporting requirements. Some states will use existing federal program guidance or performance measures to evaluate impact, particularly for on-going programs. Other states are waiting for additional guidance from federal departments or from OMB on how and what to measure to assess impact. While Georgia is waiting on further federal guidance, the state is adapting an existing system (used by the State Auditor to fulfill its Single Audit Act responsibilities) to help the state report on Recovery Act funds.

<sup>26</sup>See, OMB memoranda, M-09-10, *Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, February 18, 2009, and M-09-15, *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, April 3, 2009.

<sup>27</sup>OMB, *Information Collection Activities: Proposed Collection; Comment Request*, Federal Register – 74 Fed. Reg. 14824 (Apr. 1, 2009).

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The statewide web-based system will be used to track expenditures, project status, and job creation and retention. The Georgia governor is requiring all state agencies and programs receiving Recovery Act funds to use this system. Some states indicated that they have not yet determined how they will assess impact.

Officials in 9 of the 16 states and the District expressed concern about the definitions of jobs retained and jobs created under the Recovery Act, as well as methodologies that can be used for estimation of each.<sup>28</sup> Officials from several of the states we met with expressed a need for clearer definitions of "jobs retained" and "jobs created." Officials from a few states expressed the need for clarification on how to track indirect jobs,<sup>29</sup> while others expressed concern about how to measure the impact of funding that is not designed to create jobs. Mississippi state officials suggested the need for a clearly defined distinction for time-limited, part-time, full-time, and permanent jobs; since each state may have differing definitions of these two categories. Officials from Massachusetts expressed concern that contractors may overestimate the number of jobs retained and created. Some existing programs, such as highway construction, have methodologies for estimating job creation. But other programs, existing and new, do not have job estimation methodologies.

Some of the questions that states and localities have about Recovery Act implementation may have been answered in part via the guidance provided by OMB for the data elements as well as by guidance issued by federal departments. For example, OMB provided draft definitions for employment, as well as for jobs retained and jobs created via Recovery Act funding. However, OMB did not specify methodologies for estimating jobs retained and jobs created, which has been a concern for some states. Data elements were presented in the form of templates with section by section data requirements and instructions. OMB provided a comment period during which it is likely to receive many questions and requests for clarifications from states, localities, and other entities that can be direct recipients of Recovery Act funding. OMB plans to update this guidance

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<sup>28</sup>Recovery Act, § 3(a)(1). Non-federal entities receiving discretionary funds appropriated under the Recovery Act must report on the number of jobs created and retained, among other requirements. Mandatory and entitlement programs are excluded from this requirement. Recovery Act, div. A, title XV, § 1512.

<sup>29</sup>Indirect jobs are jobs created as a result of a demand for goods and services generated by direct funding from the Recovery Act.

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again in the next 30 to 60 days. Some federal agencies have also provided guidance to the states. The Departments of Education, Housing and Urban Development, Justice, Labor, Transportation, the Corporation for National Community Service, the National Institutes of Health, and the Centers for Medicare & Medicaid Services have provided guidance for program implementation, particularly for established programs. Although guidance is expected, some new programs, such as Broadband Deployment Grants, are awaiting issuance of implementation instructions.

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**Concluding  
Observations and  
Recommendations:  
Moving Forward to  
Clarify Recovery Act  
Roles and  
Responsibilities**

It has been a little over two months since enactment of the Recovery Act and OMB has moved out quickly. In this period, OMB has issued two sets of guidance, first on February 18 and next on April 3, with another round to be issued within 60 days. OMB has sought formal public comment on its April 3 guidance update and before this, according to OMB, reached out informally to Congress, federal, state, and local government officials, and grant and contract recipients to get a broad perspective on what is needed to meet the high expectations set by Congress and the Administration. In addition, OMB is standing up two new reporting vehicles, Recovery.gov, which will be turned over to the Recovery Accountability and Transparency Board and is expected to provide unprecedented public disclosure on the use of Recovery Act funds, and a second system to capture centrally information on the number of jobs created or retained. As OMB's initiatives move forward and it continues to guide the implementation of the Recovery Act, OMB has opportunities to build upon its efforts to date by addressing several important issues.

These issues can be characterized broadly in three categories: (1) Accountability and Transparency Requirements, (2) Administrative Support and Oversight, and (3) Communications.

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**Accountability and  
Transparency  
Requirements**

Recipients of Recovery Act funding face a number of implementation challenges in this area. The Act includes many programs that are new or new to the recipient and, even for existing programs, the sudden increase in funds is out of normal cycles and processes. Add to this the expectation that many programs and projects will be delivered faster so as to inject funds into the economy and it becomes apparent that timely and efficient evaluations are needed. The following are our recommendations to help strengthen ongoing efforts to ensure accountability and transparency.

## Single Audit

The single audit process is a major accountability vehicle but should be adjusted to provide appropriate focus and the necessary level of accountability over Recovery Act funds in a timelier manner than the current schedule. OMB has been reaching out to stakeholders to obtain input and is considering a number of options related to the single audit process and related issues.

**We Recommend:** To provide additional leverage as an oversight tool for Recovery Act programs, the Director of OMB should adjust the current audit process to:

- focus the risk assessment auditors use to select programs to test for compliance with 2009 federal program requirements on Recovery Act funding;
- provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010; and
- evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.

## Reporting on Impact

Responsibility for reporting on jobs created and retained falls to non-federal recipients of Recovery Act funds. As such, states and localities have a critical role in determining the degree to which Recovery Act goals are achieved. Senior Administration officials and OMB have been soliciting views and developing options for recipient reporting. In its April 3 guidance, OMB took an important step by issuing definitions, standard award terms and conditions, and clarified tracking and documenting Recovery Act expenditures. Furthermore, OMB and the Recovery Accountability and Transparency Board are developing the data architecture for the new federal reporting system that will be used to collect recipient reporting information. According to OMB, state chief information officers commented on an early draft and OMB expects to provide an update for further state review.

**We Recommend:** Given questions raised by many state and local officials about how best to determine both direct and indirect jobs created and retained under the Recovery Act, the Director of OMB should continue OMB's efforts to identify appropriate methodologies that can be used to:

- assess jobs created and retained from projects funded by the Recovery Act;
- determine the impact of Recovery Act spending when job creation is indirect;

- identify those types of programs, projects, or activities that in the past have demonstrated substantial job creation or are considered likely to do so in the future. Consider whether the approaches taken to estimate jobs created and jobs retained in these cases can be replicated or adapted to other programs.

There are a number of ways that the needed methodologies could be developed. One option would be to establish a working group of federal, state and local officials and subject matter experts.

#### State and Federal Data Collection

Given that governors have certified to the use of funds in their states, state officials are uncertain about their reporting responsibilities when Recovery Act funding goes directly to localities. Additionally, they have concerns about the capacity of reporting systems within their states, specifically, whether these systems will be capable of aggregating data from multiple sources for posting on Recovery.gov. Some state officials are concerned that too many federal requirements will slow distribution and use of funds and others have expressed reservations about the capacity of smaller jurisdictions and non-profits to report data. Even those who are confident about their own systems are uncertain about the cost and speed of making any required modifications for Recovery.gov reporting or further data collection.

Problems also have been identified with federal systems that support the Recovery Act as well. For example, questions have been raised about the reliability of [www.USASpending.gov](http://www.USASpending.gov) ([USASpending.gov](http://USASpending.gov)) and the ability of Grants.gov to handle the increased volume of grant applications. OMB is taking concerted actions to address these concerns. It plans to reissue USASpending guidance shortly to include changes in operations that are expected to improve data quality. In a memorandum dated March 9, OMB said that it is working closely with federal agencies to identify system risks that could disrupt effective Recovery Act implementation and acknowledged that Grants.gov is one such system. A subsequent memorandum on April 8, offered a short-term solution to the significant increase in Grants.gov usage while longer-term alternative approaches are being explored. GAO has work underway to review differences in agency policies and methods for submitting grant applications using Grants.gov and will issue a report shortly.

OMB addressed earlier questions about reporting coverage in its April 3 guidance. According to OMB there are limited circumstances in which prime and sub recipient reporting will not be sufficient to capture information at the project level. OMB stated that it will expand its current

model in future guidance. OMB guidance described recipient reporting requirements under the Recovery Act's section 1512 as the minimum which must be collected, leaving it to federal agencies to determine whether additional information would be required for program oversight.

**We Recommend:** In consultation with the Recovery Accountability and Transparency Board and States, the Director of OMB should evaluate current information and data collection requirements to determine whether sufficient, reliable and timely information is being collected before adding further data collection requirements. As part of this evaluation, OMB should consider the cost and burden of additional reporting on states and localities against expected benefits.

#### Administrative Support and Oversight

At a time when states are experiencing cutbacks, state officials expect the Recovery Act to incur new regulations, increase accounting and management workloads, change agency operating procedures, require modifications to information systems, and strain staff capacity, particularly for contract management. Although federal program guidelines can include a percentage of grants funding available for administrative or overhead costs, the percentage varies by program. In considering other sources, states have asked whether the portion of the State Fiscal Stabilization Fund that is available for government services could be used for this purpose. Others have suggested a global approach to increase the percentage for all Recovery Act grants funding that can be applied to administrative costs. As noted earlier, state auditors also are concerned with meeting increased audit requirements for Recovery Act funding with a reduced number of staff and without a commensurate reduction in other audit responsibilities or increase in funding. OMB and senior administration officials are aware of the states' concerns and have a number of options under consideration.

**We Recommend:** The Director of OMB should timely clarify what Recovery Act funds can be used to support state efforts to ensure accountability and oversight, especially in light of enhanced oversight and coordination requirements.

#### Communications

State officials expressed concerns regarding communication on the release of Recovery Act funds and their inability to determine when to expect federal agency program guidance. Once funds are released, there is no consistent procedure for ensuring that the appropriate officials in states and localities are notified. According to OMB, agencies must

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immediately post guidance to the Recovery Act web site and inform to the "maximum extent practical, a broad array of external stakeholders." In addition, since nearly half of the estimated spending programs in the Recovery Act will be administered by non-federal entities, state officials have suggested opportunities to improve communication in several areas. For example, they wish to be notified when funds are made available to prime recipients that are not state agencies.

Some of the uncertainty can be attributed to evolving reports and timing of these reports at the federal level as well as the recognition that different terms used by federal assistance programs add to the confusion. A reconsideration of how best to publicly report on federal agency plans and actions led to OMB's decision to continue the existing requirement to report on the federal status of funds in the Weekly Financial and Activity Reports and eliminate a planned Monthly Financial Report. The Formula and Block Grant Allocation Report has been replaced and renamed the Funding Notification Report. This expanded report includes all types of awards, not just formula and block grants, and is expected to better capture the point in the federal process when funds are made available.

**We Recommend:** To foster timely and efficient communications, the Director of OMB should develop an approach that provides dependable notification to (1) prime recipients in states and localities when funds are made available for their use, (2) states, where the state is not the primary recipient of funds, but has a state-wide interest in this information, and (3) all non-federal recipients, on planned releases of federal agency guidance and, if known, whether additional guidance or modifications are expected.

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Mr. Chairman, Senator Collins, and Members of the Committee, this concludes my statement. I would be pleased to respond to any questions you may have.



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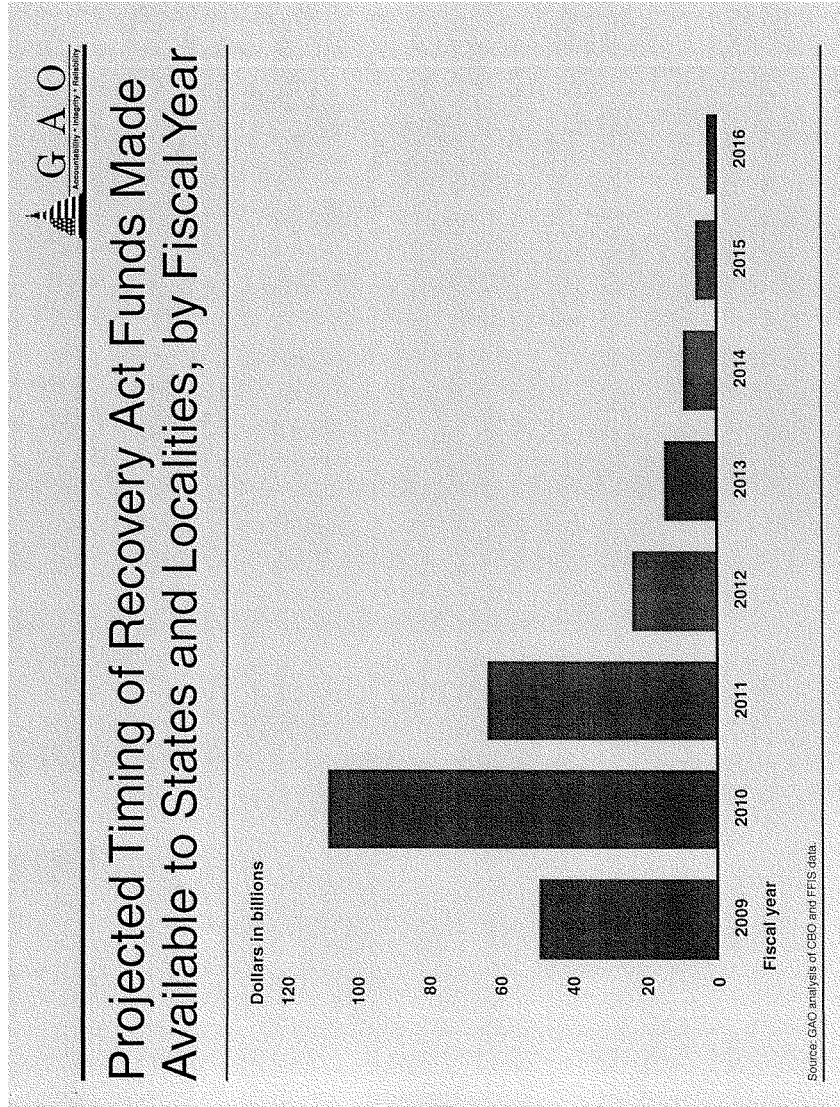
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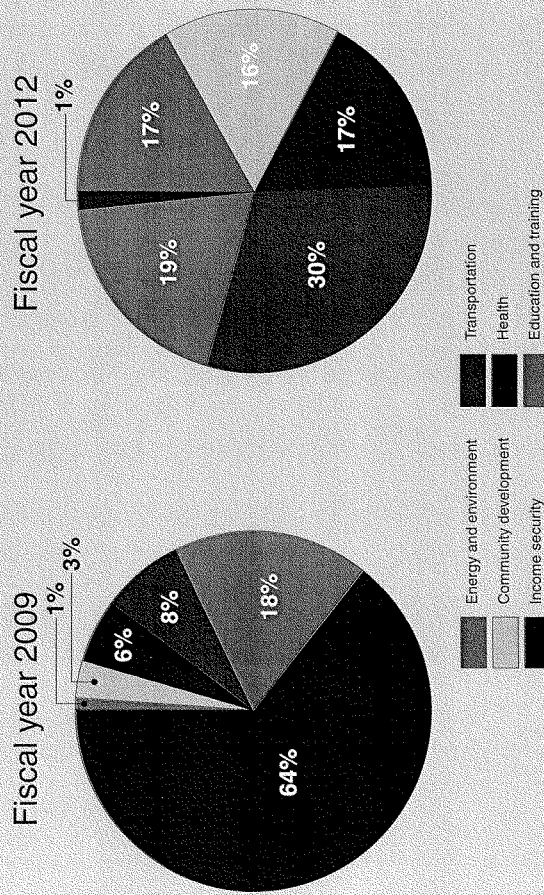
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# Composition of State and Local Recovery Act Funding, Fiscal Year 2009 versus Fiscal Year 2012



Sources: GAO analysis of CBO and FFI/S data.

NATIONAL  
GOVERNORS  
ASSOCIATION

**Testimony of Ray Scheppach, Ph.D.  
Executive Director, National Governors Association**

**Before the Committee on Homeland Security  
and Governmental Affairs  
U.S. Senate**

***“Follow the Money: State and Local Oversight of Stimulus Funding”***

**April 23, 2009**

Chairman Lieberman, Ranking Member Collins, members of the committee, on behalf of the nation's governors, thank you for the opportunity to appear before you today to discuss state efforts to implement the American Recovery and Reinvestment Act (ARRA).

#### Background

The economic conditions governors face in their states are unprecedented. Earlier this year NGA estimated that state budget shortfalls for fiscal years 2009 and 2010 would top \$230 billion as a result of falling revenues from the faltering economy. These shortfalls mean that governors must cut services or develop new sources of revenues to meet state balanced budget requirements -- actions that could slow an economic turnaround.

Furthermore, history has shown that states experience the worst fiscal conditions the year after a national recession ends. With economists forecasting that the economy will continue to contract through 2009, and unemployment rates increasing into 2010, governors are planning for difficult financial times through fiscal year 2011 and possibly 2012.

As a result, NGA issued a paper with recommendations regarding a possible federal stimulus bill to spur the economy and put people back to work. NGA's recommendations included countercyclical funding for states to reduce the need for cuts to services or tax increases; investments in infrastructure to create jobs and promote economic competitiveness; and funding for safety net programs to help individuals impacted by the downturn.

Governors also met with then President-elect Obama and Vice President-elect Biden to discuss the economy and encouraged the incoming administration to hold governors accountable for the use of federal recovery funds. Specifically, governors voiced support for use-it-or-lose-it criteria to ensure rapid deployment of federal dollars.

The ARRA reflects each of these recommendations. It provides more than \$135 billion to states in countercyclical funds through Medicaid and education. It invests in core infrastructure including highway, transit and water systems. It also provides additional funds to extend unemployment assistance and other benefits for individuals and families. All told, of the \$787 billion provided by the ARRA, more than \$246 billion will go to or be administered by states. This places states, and governors, on the front lines partnering with the federal government to make the ARRA work.

To one extent this hearing is premature. Having just passed in February, most ARRA funds remain in the hands of the federal government, and the federal agencies charged with distributing the funds are still developing the guidance and rules necessary for states to implement the act.

On the other hand, this hearing is well-timed because meeting the levels of transparency and accountability called for by the ARRA will take an extraordinary level of cooperation and coordination between federal agencies and state and local governments. If developed properly, federal and state rules should help spend federal funds efficiently and prevent waste, fraud and abuse. If, however, federal, state and local efforts are not well coordinated, funds may be spent too quickly or on projects that do not maximize job creation or economic growth.

As this committee begins its review of federal and state actions to implement the ARRA, NGA offers the following recommendations:

- **Coordinate and streamline reporting requirements and oversight**  
Congress and the Administration should avoid duplicative or unnecessary reporting requirements by sharing information and developing common definitions to make state reporting easier and more usable.
- **Provide resources for accountability and transparency**  
Millions of dollars were provided to federal Inspectors General to conduct oversight and prevent waste, fraud and abuse. Flexibility in the use of ARRA funds by states to meet transparency and accountability standards is necessary to develop and improve state systems and capabilities to meet ARRA requirements.
- **Allow time for planning**  
The ARRA's objective of spending money quickly must be tempered with the objective of spending federal taxpayer dollars wisely. Congress and the Administration should provide states flexibility to organize and plan after federal rules are finalized to ensure proper handling and priority setting at the state level. This would allow ready-to-go states to move forward immediately and provide others time to build capacity to meet ARRA requirements.
- **Communicate with and through Governor's Offices**  
The ARRA provides states and governors with central responsibility for using and administering federal recovery funds. Federal officials should therefore ensure that the governor's office is kept informed of all federal spending and activities that occur in a state.

#### The State Role

During any economic downturn, states are key players from three major perspectives. First, they administer most of the safety net programs in the United States. The four major programs that can both help stabilize the economy and provide benefits to individuals in need are 1) Medicaid, 2) welfare benefits, 3) unemployment compensation and 4) food stamps. All of these are federal-state programs that receive major federal funding. Second, states can quickly create jobs in the short-run through infrastructure investment such as highways, transit projects and water and sewer system modernization. States are able to do this quickly because states administer many infrastructure programs and have detailed information regarding unmet needs. Third, because of balanced budget requirements<sup>1</sup>, states typically react to downturns by cutting spending and raising taxes, which make the downturn more severe. Direct federal government payments to states to help offset these actions is therefore one of the most powerful countercyclical actions the federal government can take.

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<sup>1</sup> All but one state has a balance budget requirement.

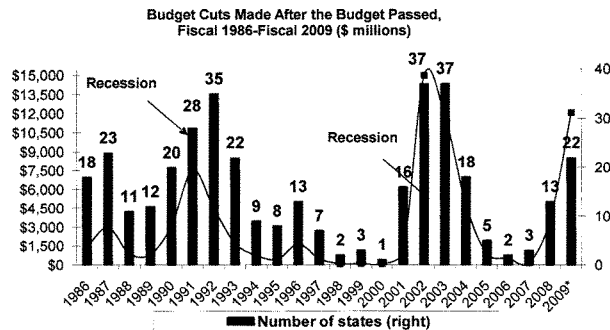
### State Shortfalls

A survey of state fiscal conditions late last year projected state shortfalls of \$230 billion for FY 2009 and FY 2010. My best estimate today is that without ARRA dollars, states would face budget gaps of \$300 to \$350 billion through fiscal year 2011. Tax collections continue to trend downward with sales tax, corporate business tax and personal income tax revenue all staying negative during the first quarter of 2009. These revenues will be further depressed by the lack of capital gain tax revenues resulting from the sell-off in the stock market. Income tax revenues are likely to dip most after unemployment peaks, which could be as late as mid-2010.

### State Impacts Lag the Downturn

Unfortunately, even with distribution of ARRA funds, states' fiscal picture will continue to deteriorate over the next two years. When the economy slows, state sales tax revenues decline as reductions in personal consumption often lead downturns. Rising unemployment is the next sign, which in turn leads to declines in state personal and corporate income tax revenues. The increase in unemployment also often leads to increases in the demand for food stamps, unemployment benefits and Medicaid payments, which is currently about 21 percent of state budgets.

The lag effect on states was evident in each of the last two recessions. The recession that ended in 1991 resulted in 28 states cutting budgets that year. States, however, continued to experience the recession's impact and in 1992, 35 states cut budgets. Similarly in 2001, when the most recent recession ended, 16 states cut budgets. However, 37 states cut budgets in each of the next two years—2002 and 2003. (See Chart: Budget Cuts Made After the Budget Passed). If the current downturn continues and follows the path of past recessions, most states will face budget shortfalls in 2010, 2011 and possibly 2012.



Managing the American Recovery and Reinvestment Act

With more than \$246 billion in recovery funds flowing to or through states, governors have taken an aggressive approach to managing ARRA funds and programs. Governors are keenly aware of the inherent tension the ARRA's objectives pose for states: spend funds quickly; target funds effectively; and prevent waste, fraud and abuse. These objectives must also be measured against the fact that ARRA funds are temporary and cannot be counted on to fund long-term reforms or benefit expansions.

From a state perspective, it is critical to think in terms of the ARRA's various categories of spending because they have very different intents and many require different management structures, reporting requirements, and the involvement of state legislatures. Four categories are particularly important.

a. Countercyclical Funds

There are two major categories of the countercyclical funds, which are the most flexible funds. First, there is the \$87 billion in estimated federal increase in Medicaid funds. Second, there is \$48 billion in the State Fiscal Stabilization Fund, which includes \$8.8 billion that can be used for any purpose as well as education, and \$39.5 billion that must be used for elementary, secondary and higher education. Because education averages about 46 percent of state budgets, it provides considerable fiscal relief. It is important to note that local school districts will also receive an additional \$25 billion in Title I and special education grants for education. The combination of Medicaid enhancements and the State Stabilization Fund means that the flexible funds provided under the act total about \$135 billion.

This \$135 billion is critical for states because it can be used to offset states' projected \$300-\$350 billion in shortfalls through fiscal year 2011. The new dollars are an appropriate amount that will help stabilize the economy and offset the most draconian cuts, but will keep the pressure on states to continue to consolidate, streamline and downsize state government. Already ARRA funds have had a positive economic impact: states are postponing planned cuts and tax increases for fiscal year 2010.

Although the allocation of countercyclical funds across states could be better targeted, the Medicaid formula does account for economic stress, and therefore many of the states with the worst underlying economies get a larger allocation of funds. There are only a few small states—generally those that produce energy—that may receive funds above their needs. For most states, these flexible federal funds are far short of need. The fact that the Medicaid funds were retroactive to October 1, 2008, was extremely helpful in allowing states to postpone planned cuts. It is important to note, however, that even after the recovery package, states will continue to face a shortfall of more than \$200 billion over the next three years, and will therefore continue to reduce spending and consider increasing taxes to balance their budgets.

b. Appropriated Programs

The ARRA contains a significant number of direct appropriations into existing federal-state programs, which run the gamut from \$27.5 billion for highways to \$1 billion for community services block grants to \$3.1 billion for state energy grants. States have little flexibility here and must spend these additional funds in the specified program areas. Many of these grants are



formula while others are discretionary or competitive grants. This category includes about 50 programs, and in many cases, states are required to obligate and spend these funds quickly to create jobs.

c. Safety Net

The ARRA also expands on a number of safety net programs such as transitional Medicaid assistance, food stamps and unemployment insurance. Most of these programs will require states to make decisions regarding new eligibility and benefit levels, which may require state legislative changes as well as major changes to business processes and management information systems. Safety net funds are generally spent quickly by recipients and, thus, have a positive macroeconomic impact.

d. Foundations for Economic Development

The ARRA also provides funds for several long-run investments with the potential for economic growth including: alternative energy and smart grid technology; Health IT; broadband deployment and access; high-speed rail; and funding for research and development. Most of the funding in these areas is for new programs that require significant planning and development by both the federal government and states. Maximizing these dollars requires a coordinated approach, governance structure and clear strategic goals. More than any other type of funding under the ARRA, these funds are targeted towards establishing capabilities to develop and promote long-term economic growth.

Accountability and Transparency

The legislation contains numerous provisions to ensure that the appropriated funds are spent as intended by Congress. As a result, state activities will be subjected to extensive public scrutiny and to enhanced oversight by a variety of federal entities, including federal program managers, agency inspectors general, and the Government Accountability Office (GAO). Federal efforts are being coordinated by the newly established Accountability and Transparency Board, which is charged with preventing potential waste, fraud and abuse and is made up of inspectors general from several federal agencies.

In addition, the legislation requires the board to operate the Web site, [www.recovery.gov](http://www.recovery.gov), as a portal or gateway to key information related to recovery efforts and to provide a window to other government Web sites with related information. States will be required to use this Web site to post information on the use of both operational funding and infrastructure investments. The required information is generally more detailed than mandated by current statutes including:

- Descriptions of the intended use of the funds;
- Impact on job development and preservation; and
- Copies of individual grants and contracts.

Finally, the legislation includes substantial increases in the appropriations for the GAO and departmental inspectors general. It also requires grantees to provide federal reviewers with unfettered access to state records and establishes new whistle-blower protections, including the authority for federal inspectors general to review and decide claims regarding retaliation. GAO has already identified and initiated reviews of implementation activities in 16 states.

#### Challenges for States

Governors expect to be held fully accountable for their use of ARRA funds. To best achieve these objectives, governors are acting to build or expand a capacity to:

- Plan and establish priorities;
- Obtain necessary legislative and public support;
- Coordinate the interaction between state and federal agencies;
- Oversee state agency implementation, including coordination and collaboration across agency and program lines;
- Expand workforce capacity to develop and monitor a rapid growth in contracts;
- Ensure compliance with grant requirements, including transparency and accountability provisions; and
- Facilitate local government and private sector opportunities to utilize federal grant and loan programs to the maximum extent.

#### State Planning

Governors understand that thoughtful planning and skilled implementation are necessary to achieve the full benefit of the opportunities encompassed in the ARRA. Planning is required to ensure that new spending is timed to provide necessary resources over the duration of the recession and initial recovery. Failure to plan early for the next two to three years could worsen the out-year impact because states may be hard pressed to meet service expectations or commitments once ARRA funds are exhausted.

Planning is also vital to ensure that available funds are used strategically to address both short-term needs of individuals adversely affected by the recession and opportunities to invest in future economic growth. A thoughtful planning process that involves multiple stakeholders at an early stage can help both to identify priorities and the opportunities to coordinate a variety of funding sources to help achieve broader goals. That process also can help identify and address issues relating to the sustainability of programs and services that may be initiated or expanded under the ARRA.

To organize ARRA planning and implementation efforts, states have tended to organize around a single individual or task force. These single points of authority provide the broad perspective and ability to coordinate funding across stove-piped federal programs to maximize job creation and economic growth. These are also generally the offices that will be in charge of fulfilling the ARRA's extensive public reporting provisions.

#### Good news about the ARRA

Although the Act is only a couple of months old, there is positive news.

1. The Administration, individual agencies and OMB have provided a substantial amount of guidance and funds are beginning to flow.
2. Every governor has appointed key staff to serve as their leads and many have appointed task forces with private sector and community leaders.

3. OMB, GAO and individual agencies have been accessible and cooperative in working with state organizations to solve problems as they become known.

4. Perhaps most important, the recovery package was well timed. The history on fiscal policy changes to stimulate economic growth has been very poor. Specifically, past stimulus packages have generally come too late and the impact is often after the economy has already turned up. Given the length of this downturn, however, this package will likely moderate the downturn in two important ways. First, the flexible or countercyclical funds have already allowed many states to postpone planned budget cuts or tax increases. This has had the positive impact of limiting the magnitude of the downturn. Second, the economy is still deteriorating although more slowly, and funds from the stimulus are now being spent. Thus, this recovery package should be helpful over the next year in both limiting the downturn and perhaps helping the economy to turn the corner. Unlike most previous fiscal policy changes, the ARRA was not too late.

#### Ongoing Challenges

While there is some very positive news, it is also true that governors and states face a number of challenges.

1. The first major challenge for states is to spend the money quickly to maximize job creation while maintaining program stability and efficiency and filling a budget gap that will last at least three years. The three year projection is based on the assumption that it will take two years for GDP to return to the 2008 level and a third year, based on historical observations that the year after a recession is generally the most difficult fiscal period for states. Given that all of the economic stimulus funds are temporary, it will be extremely difficult for states to spend funds quickly, fill a three-year budget gap and maintain program stability and efficiency.

2. States will be accountable not only to the various agencies and OMB, but also the new Recovery Act Transparency and Accountability Board and GAO. Since OMB has yet to publish the final reporting requirements, it is difficult to determine the degree of burden faced by states and ARRA fund recipients. Governors' greatest concern is that the federal agencies various requirements for information will not be consistent or coordinated further burdening states to meet duplicative requirements. Requests for information from congressional committees are also an issue because to date they have not been coordinated with reporting requirements from the Administration. NGA recommends that future congressional oversight activities rely primarily upon the massive volume of information the federal government will receive from states rather than requesting new or different information about the same projects from states.

3. While the ARRA provided ample funding for federal oversight activities, little was provided for states. Those funds that are available are linked to specific programs rather than applying to all ARRA funds. Governors are encouraged by suggestions that OMB is working on guidance to allow some limited use of ARRA funds for meeting ARRA reporting and transparency requirements, but until that time the lack of funding for accountability remains a major concern.

4. A primary focus of the ARRA is to save and create jobs. Yet estimating the direct jobs created and the number of jobs saved will be very difficult. The Administration needs to establish more specific guidance in this area to ensure proper data collection and accurate reporting. Even with additional guidance, however, the jobs data will have limited value to make comparisons across projects or states.

5. States will be challenged in those program areas where there was not an existing program or where the budget increases were dramatic. The weatherization program is a primary example as states will have to scale up capacity to manage and distribute a massive influx of funds over the next 24 months.

6. States need time to plan and execute in the five areas (Health IT, broadband, high speed rail, R&D and alternative energy and smart grid) for long-run growth. The focus of these programs is different from short-run stimulus programs and thus effective and efficient planning, as opposed to accelerating spending, should be the priority.

7. Most states have cut budgets over the last two years and therefore have less capacity to execute significant increases in spending or take advantage of new programs requiring state matching funds. States will rebuild capacity to take advantage of ARRA opportunities, but it will take time.

8. The transparency and accountability at the heart of the ARRA is quite different from that of existing programs. Consequently, it will require tracking systems and capabilities that may differ from those currently employed by states. Existing state information systems may need to be upgraded or replaced to meet ARRA standards.

9. From the public's perspective, governors are responsible for all funds that go to a state regardless of whether they flow through a state or go directly to a quasi-independent agency, (e.g., a port authority), or a local government. In order for governors to effectively manage ARRA implementation for their states, governors must be notified in a timely manner of all investments made in their individual states.

Mr. Chairman, I appreciate the opportunity to appear before you today to discuss implementation of ARRA. Again, I want to stress the fact that we are very early in the implementation process and therefore these comments must be viewed as preliminary. I look forward to working with you as you continue your review of ARRA funds and the actions of states to put people back to work, make our nation more competitive and speed economic recovery.

To strengthen  
and promote  
cities as centers  
of opportunity,  
leadership, and  
governance.



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**Written Testimony of**

**Carolyn M. Coleman**  
Director, Federal Relations  
National League of Cities

**Before the  
U.S. Senate Committee on  
Homeland Security and Government Affairs**

**Washington, DC  
Wednesday, April 23, 2009**

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Thank you Chairman Lieberman, Ranking Member Collins, and members of the U.S. Senate Homeland Security and Government Affairs Committee. I am pleased to be here this morning to discuss the responsibilities for accountability and transparency placed on local governments under the American Recovery and Reinvestment Act of 2009 and to summarize efforts undertaken, thus far, to comply with those responsibilities, as well as some of the challenges that lie ahead. I am Carolyn Coleman, Director, Federal Relations, for the National League of Cities. NLC is the nation's oldest and largest organization devoted to strengthening and promoting cities as centers of opportunity, leadership and governance. NLC is a resource and advocate for 18,000 cities, towns and villages, representing more than 218 million Americans.

As the economic engines of the country, cities play a key role in ensuring the resources in the ARRA achieve the intended purpose of boosting our economy and saving and creating jobs. At this critical time, the future of our country and the places we call home are inextricably intertwined. "This bold legislation unites all levels of government in an unprecedented effort to get our country back to work and provides new resources that will help us create and preserve good jobs, strengthen the economy, and provide long-lasting benefits to our communities," said NLC President Kathleen Novak, mayor, Northglenn, Colorado, upon the bill's signing. In anticipation of ARRA, in February, NLC began mobilizing resources and programmatic opportunities organization-wide to help local government leaders prepare to receive and invest recovery funds in ways consistent with the Act.

**Congressional City Conference**

In March, NLC hosted its annual Congressional City Conference in Washington, D.C. Attended by over 2,500 local government leaders from across the country, the conference program featured general sessions focused on the ARRA, as well as workshop opportunities for local leaders to discuss the Act and its requirements with federal agency representatives. (*See attachment 1*)

**Webcasts**

In addition to the Conference, NLC has hosted three ARRA webcasts for local elected officials and city staff to learn about programs funded in the ARRA and is planning for two additional webcasts during the month of May. By our estimates, these webcasts, which are archived for viewing on NLC's website, [www.nlc.org](http://www.nlc.org), are *each* reaching 4,000 – 5,000 listeners. We believe that, as the federal government, including the Government Accountability Office (GAO) and the Office of Management and Budget (OMB), releases additional guidance regarding the ARRA reporting requirements, the webcast technology will be an important tool for rapid dissemination of the information, which will help expedite local government efforts to comply with those requirements.

**Recovery Coordinators and Advisors Network**

On April 22, 2009, NLC launched the ARRA Recovery Coordinators and Advisors Network (RCAN), a national peer learning network, intended for mayors and their senior staff to share information, insights, and lessons learned regarding the reporting requirements and strategies to fully leverage federal economic recovery resources in a way that creates and retains jobs and

serves as a catalyst for long-term benefits for all communities. Importantly, RCAN also will serve as a rapid-response network to communicate with federal officials regarding the implementation status of various ARRA-funded programs and challenges local governments may be experiencing. So far, the network consists of 50 – 55 cities and more are expected to participate as this initiative gets underway.

In addition to these efforts, NLC looks forward to continuing the dialogue regarding the Act's reporting requirements and the development of future requirements with representatives from the White House, GAO, OMB, the Recovery Accountability and Transparency Board, and representatives from various federal agencies, including the Departments of Housing and Urban Development, Transportation, Justice, Energy, and Labor, and the Environmental Protection Agency.

Before and since the ARRA was enacted, cities and towns have been taking steps to ensure compliance with its accountability and transparency responsibilities. Like the federal government, local governments are developing websites to educate their residents about the ARRA and to ensure transparency and accountability in the decision-making process.

Since the legislation's passage, the City of Reno, Nevada, has launched a webpage dedicated to the ARRA on its website, [www.cityofreno.com/recovery](http://www.cityofreno.com/recovery), that contains information about the City's uses of ARRA funds, job creation, infrastructure improvements, and requests for proposals for ARRA funds. The page has a link to the State of Nevada Recovery page, the federal recovery website, as well as the legislation. In a future enhancement, the page will also



have a link to the city's financial department, so the public can track the expenditure of these funds.

Similarly, in New York City, *NYCStat Stimulus Tracker*, a comprehensive and interactive Stimulus Tracker Web site is under development. It will provide extensive detail and access to information about the use of federal stimulus/recovery funds in New York City and will include features such as:

- A detailed accounting for each funding source, including how funds are distributed to building projects and other City programs.
- Key performance measures - such as jobs created - showing how these projects and programs benefit the City.
- Details of the procurement and contracting process where applicable - such as the start and end dates of construction projects, and the status of contracting steps for outsourced projects.
- A locator map to identify key initiatives in each borough and neighborhood.

In another example, the city of Boise, Idaho, launched a webpage: [Accountable Boise](#).

According to Mayor Dave Bieter, Accountable Boise is designed to provide detailed information regarding local projects financed through the ARRA. "Our goal is transparency and accountability, to make sure that every dollar is spent on worthwhile projects that put Americans to work and help lead the economic recovery," Bieter said.

In addition to these individual city efforts, the cities of Kansas City, Missouri; Detroit, Michigan; Denver, Colorado; Cleveland, Ohio; Tempe, Arizona; Chicago, Illinois; and state municipal associations in Maine, Michigan, and South Carolina are among the many devoting sections of their web pages to federal recovery efforts.

In addition to websites, countless local governments of all sizes are establishing working groups with lead coordinators, in some cases new hires and in some cases existing employees, who meet on a regular basis to manage and oversee their overall ARRA efforts, while others have adopted a less centralized approach.

For example, in Providence, Rhode Island, in February, Mayor David N. Cicilline signed an executive order establishing a set of guidelines and priorities to ensure federal dollars authorized under ARRA are spent in the most strategic and timely manner. The executive order also created a 22-member team to identify opportunities for infrastructure improvement and job creation and to create a transparent system for tracking resources and expenditures. *(See attachment 2)* In Indianapolis, the Mayor's office is overseeing implementation of the ARRA with individual city department grants and fiscal management resources augmenting existing grants tracking systems or developing new tracking systems for ARRA funds.

To help local governments comply with their ARRA responsibilities, the federal government has provided several types of assistance and guidance. As of today, the majority of the federal agencies with responsibility for ARRA funding that will be distributed to local governments have released official guidance for those funding programs. (We believe that guidance on programs under HUD's jurisdiction will be released imminently.) In addition, federal officials

are providing assistance to local government leaders through conferences or meetings convened by various entities.

On March 18, 2009, the Vice President hosted an ARRA Implementation Conference at the White House for local government officials that featured representatives from the Recovery Accountability and Transparency Board, OMB, and the federal agencies with jurisdiction over ARRA programs. In addition to federal government efforts, local government leaders also are convening recovery information meetings in their local jurisdictions and inviting federal agency representatives to attend and brief the leaders on the various ARRA programs and requirements. The Municipal Association of South Carolina hosted such a meeting in Columbia, South Carolina, earlier this month. Also, besides the Washington headquarters offices, some federal agency regional offices have been an important source of ARRA information to local governments.

In terms of effectiveness, we understand and appreciate the challenges for the federal government in providing precise information about the ARRA's requirements, particularly given the accelerated timetables associated with implementation. In light of the evolving nature of the ARRA implementation process, we believe that the federal government's efforts to provide assistance and guidance will be more effective as OMB continues to clarify and enhance reporting requirements.

As local governments begin implementing the ARRA in communities across the country, important challenges lie ahead. The ARRA covers new ground, not just in the level of funding but with its accountability and transparency mandates. Importantly, these reporting requirements

are not buried at the back of the bill but featured immediately after the summary of its major provisions.

While the ARRA was premised on providing additional funding to existing federal programs as the fastest means to get the money working by avoiding start-up time associated with new federal programs, the level of accountability is new, yet the resources for compliance are greatly lacking.

The Act creates the Recovery Accountability and Transparency Board to review management of the recovery funds and appropriates resources for the Board to fulfill its responsibilities. The seven-person board, composed of federal inspectors general (IGs) and deputy cabinet secretaries, is also charged with providing early warnings of any problems. We have met its newly appointed Chair, Earl Devaney, with whom we expect to work very well.

The ARRA also tasks the GAO and Federal Agency IGs with carrying out specific oversight roles and reporting requirements and allocates resources for them to this important work.

We certainly agree with the President when he said at his inaugural: "Those of us who manage the public's dollars will be held to account – to spend wisely, reform bad habits, and do our business the right way – because only then can we restore the vital trust between a people and their government" and expect no less than such heightened scrutiny given the magnitude of the investment called for by the ARRA.

However, local governments receive no specific allocation of ARRA oversight resources and are only able to leverage small amounts of administrative (or indirect costs) within grants, which

could impact the competitiveness of the grant application or discourage local governments from pursuing ARRA resources.

In addition to the challenge of ensuring adequate administrative oversight capacity, ambiguity in terms of performance measures and compliance requirements could be a challenge to the extent it exposes good projects funded by the ARRA to unjustified, misinformed, hostile public criticism. Additionally, lack of clarity in the reporting requirements will negatively impact the ability of all levels of government to demonstrate to the public progress towards the achievement of the ARRA goals.

Accordingly, to help achieve the Act's goals with the intended accountability and transparency in the decision-making process, we believe cities specifically would benefit from additional federal guidance with respect to the types of projects eligible for ARRA funding and from federal guidance with the definition of calculation of jobs, both retained and created. Additionally, we believe the important effort to report on jobs would benefit greatly from a common set of tools – developed by the federal government and made available to states, local governments, and other appropriate ARRA funded recipients.

Further, we recommend that additional consideration be given to providing an additional allocation of resources to local governments to ensure compliance with the ARRA and that the funds made available through the Act are able to be used for their intended purposes.

In closing, cities have always been the seat of innovation in this country and stand ready to work in partnership with the federal government (and the states) as we together help turn around our economy.

Thank you for the opportunity to appear here this morning. I would be happy to answer any questions.

**Congressional City Conference to Focus on Impact of Federal Economic Recovery Package on Cities**  
by Carolyn Coleman and Tricia Dwyer-Morgan

# 2009 Annual • Congressional City Conference

Marriott Wardman Park • Washington, DC • March 14 -18, 2009

Next month's Congressional City Conference will focus on how cities can get the most out of the economic recovery package signed into law by President Obama last week.

The conference will feature general sessions, workshops and other sessions with the latest information from federal agency representatives and other technical experts who can help local officials learn how to bring these recovery dollars home and how to best leverage them with other resources to make a difference in these troubling economic times.

"We understand that you are watching every dollar and you need to be concerned about traveling to meetings when budgets are being cut," said NLC President Kathleen Novak, who was present at the signing of the economic recovery bill. "However, it is also important for your constituents to know that by attending the NLC Congressional City Conference you are making sure you are taking advantage of an opportunity to learn about these unprecedented resources available to your community to create jobs and improve fundamental infrastructure."

The \$787 billion American Recovery and Reinvestment Act aims to spur millions of jobs through massive investments in transportation, energy, education and health care. The economic recovery package contains resources for cities to create jobs and resources for improvements to roads, bridges, sewer and water facilities and housing.

In addition to conference activities, NLC TV, NLC's Internet TV channel, will hold a webcast, "The Federal Recovery Package: What's In It for Cities and How to Access the Resources," this Wednesday, February 25, from 3:00 to 4:00 p.m. EST. To participate, go to [www.NLCTV.org](http://www.NLCTV.org) and click on the webcast event page under "Coming Up."

Resources targeted to local governments in the package will become available from three sources: (1) through state agencies; (2) through federal formula programs; and (3) through federal agency discretionary grant programs. But local elected officials will have to take action to access these resources.

The conference, taking place March 14-18 at the Marriott Wardman Park in Washington, D.C., will help local officials do just that, as well as provide opportunities to lobby federal officials on issues important to their cities.

In addition to several sessions on the stimulus package, the annual legislative conference will provide a lineup of key Congressional and Administration leaders sharing their priorities for the coming year.

Workshops on issues such as public safety, sustainability, the housing and mortgage crisis, health care reform and youth and families will provide background information for city officials on key pieces of legislation being considered by Congress. Mini plenary sessions will offer the opportunity for a more in-depth look at some of these issues.

The Congressional City Conference also gives local officials the opportunity to network and learn from each other through lunch sessions and other meetings. Leadership Training Institute seminars and NLC meetings will take place before the general conference program.

For the latest information on the conference and to register, visit [www.NLCCongressionalCityConference.org](http://www.NLCCongressionalCityConference.org).

Attachment 1



Executive Office, City of Providence, Rhode Island  
DAVID N. CICILLINE  
MAYOR

Date: February 27th, 2009

For Immediate Release

Contact: Karen Southern, Press Secretary  
(401) 421-2489 x 752  
[ksouthern@providenceri.com](mailto:ksouthern@providenceri.com)

PRESS RELEASE

## **MAYOR ESTABLISHES TRANSPARENT PROCESS TO MAXIMIZE ECONOMIC RECOVERY REINVESTMENT FUNDS**

**Executive order sets priorities and names 22-member team to ensure funds are invested  
strategically and expeditiously**

**PROVIDENCE** – Mayor David N. Cicilline today signed an executive order establishing a set of clear guidelines and priorities to ensure federal dollars authorized under the American Recovery and Reinvestment Act (ARRA) are spent in the most strategic and timely manner. The executive order also creates a 22-member team to identify opportunities for infrastructure improvement and job creation and to create a transparent system for tracking resources and expenditures.

"It's critically important that we maximize these funds to their fullest potential to create jobs, rebuild our infrastructure and get our economy moving again," said Mayor Cicilline. "The executive order that I signed today will ensure that every single dollar is accounted for and invested wisely as we work towards strengthening our economy and ensuring the long-term

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prosperity of our city and state.”

In addition to setting out a transparent process for accurately accounting for the expenditure of funds under the ARRA, the executive order also underscores the importance of building a proactive, productive partnership with the State to ensure the funding is utilized in the most effective manner.

The City’s priorities for the ARRA funds include:

- Increase employment and access to job training
- Repair and modernize infrastructure and transit
- Enhance long-term, sustainable economic development potential
- Provide assistance and economic relief to Providence families
- Strengthen education and public safety

Providence’s 26-member American Recovery & Reinvestment Act team will meet regularly to identify opportunities for investment, track resources and report on the results of those investments. The ARRA team is led by Policy & Legislative Affairs Director Matthew Stark and includes an ARRA project coordinator, an ARRA compliance officer, ARRA analysts, the City’s chief of Administration, chief of Operations, the director of Planning & Development, the director of Public Works, the chief engineer of Providence Water, Providence Schools superintendent, Police chief, Fire chief, acting director of Public Property, director of the Providence/Cranston Workforce Investment Board, director of the Providence After School Alliance (PASA) and the director of the Mayor’s Substance Abuse Prevention Council, the director of Emergency Management, director of Pathways to Opportunity, director of the Public Housing Authority, director of Provstat and the director of ProCap.

Attachment 2

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**GAO**

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**United States Government Accountability Office**  
**Report to Congressional Committees**

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**April 2009**

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**RECOVERY ACT**

**As Initial  
Implementation  
Unfolds in States and  
Localities, Continued  
Attention to  
Accountability Issues  
Is Essential**



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**GAO-09-580**



Highlights of GAO-09-590, a report to Senate and House Committees on Appropriations, Senate Committee on Homeland Security and Governmental Affairs, and House Committee on Oversight and Government Reform

### Why GAO Did This Study

The American Recovery and Reinvestment Act of 2009 (Recovery Act) is estimated to cost about \$787 billion over the next several years, of which about \$280 billion will be administered through states and localities. The Recovery Act requires GAO to do bimonthly reviews of the use of funds by selected states and localities. In this first report, GAO describes selected states' and localities' (1) uses of and planning of Recovery Act funds, (2) accountability approaches, and (3) plans to evaluate the impact of funds received. GAO's work is focused on 16 states and the District of Columbia—representing about 65 percent of the U.S. population and two-thirds of the intergovernmental federal assistance available through the Recovery Act. GAO collected documents from and interviewed state and local officials, including Governors, "Recovery Czars," State Auditors, Controllers, and Treasurers. GAO also reviewed guidance from the Office of Management and Budget (OMB) and other federal agencies.

### What GAO Recommends

GAO makes a number of recommendations, which are discussed on the next page. In general, OMB concurred with the overall objectives of our recommendations and plans to work with GAO to further accountability for these funds.

View GAO-09-590 or key components. For more information, contact J. Christopher Mihm at (202) 512-6806 or mihmj@gao.gov.

April 2009

## RECOVERY ACT

### As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues Is Essential

#### What GAO Found

##### Uses and Planning for Recovery Act Funds

About 90 percent of the estimated \$49 billion in Recovery Act funding to be provided to states and localities in FY2009 will be through health, transportation and education programs. Within these categories, the three largest programs are increased Medicaid Federal Medical Assistance Percentage (FMAP) grant awards, funds for highway infrastructure investment, and the State Fiscal Stabilization Fund (SFSF). The funding notifications for Recovery Act funds for the 16 selected states and the District of Columbia (the District) have been approximately \$24.2 billion for Medicaid FMAP on April 3, \$26.7 billion for highways on March 2, and \$32.6 billion for SFSF on April 2.

##### Increased Medicaid FMAP Funding

Fifteen of the 16 states and the District have drawn down approximately \$7.96 billion in increased FMAP grant awards for the period October 1, 2008 through April 1, 2009. The increased FMAP is for state expenditures for Medicaid services. The receipt of this increased FMAP may reduce the state share for their Medicaid programs. States have reported using funds made available as a result of the increased FMAP for a variety of purposes. For example, states and the District reported using these funds to maintain their current level of Medicaid eligibility and benefits, cover their increased Medicaid caseloads—which are primarily populations that are sensitive to economic downturns, including children and families, and to offset their state general fund deficits thereby avoiding layoffs and other measures detrimental to economic recovery.

##### Highway Infrastructure Investment

States are undertaking planning activities to identify projects, obtain approval at the state and federal level and move them to contracting and implementation. For the most part, states were focusing on construction and maintenance projects, such as road and bridge repairs. Before they can expend Recovery Act funds, states must reach agreement with the Department of Transportation on the specific projects; as of April 16, two of the 16 states had agreements covering more than 50 percent of their states' apportioned funds, and three states did not have agreement on any projects. While a few, including Mississippi and Iowa had already executed contracts, most of the 16 states were planning to solicit bids in April or May. Thus, states generally had not yet expended significant amounts of Recovery Act funds.

##### State Fiscal Stabilization Fund

The states and D.C. must apply to the Department of Education for SFSF funds. Education will award funds once it determines that an application contains key assurances and information on how the state will use the funds. As of April 20, applications from three states had met that determination—South Dakota, and two of GAO's sample states, California and Illinois. The applications from other states are being developed and submitted and have

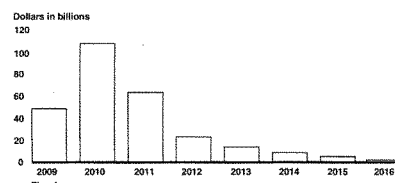
United States Government Accountability Office

## Highlights of GAO-09-580 (continued)

not yet been awarded. The states and the District report that SFSF funds will be used to hire and retain teachers, reduce the potential for layoffs, cover budget shortfalls, and restore funding cuts to programs.

This report contains separate appendixes on each of the 16 states and the District that discuss the plans and uses of funds in these three major programs as well as selected other programs that are receiving Recovery Act funds.

Planning continues for the use of Recovery Act funds. The figure below shows the projected timing of funds made available to states and localities.



Source: GAO analysis of CBO and FFIS data.

State activities include appointing Recovery Czars; establishing task forces and other entities, and developing public websites to solicit input and publicize selected projects. In many states, legislative authorization is needed before the state can receive and/or expend funds or make changes to programs or eligibility requirements.

#### Accountability Approaches

GAO found that the selected states and the District are taking various approaches to ensuring that internal controls to manage risk up-front; they are assessing known risks and developing plans to address those risks. However, officials in most of the states and the District expressed concerns regarding the lack of Recovery Act funding provided for accountability and oversight. Due to fiscal constraints, many states reported significant declines in the number of oversight staff—limiting their ability to ensure proper implementation and management of Recovery Act funds. State auditors are also planning their work including conducting required single audits and testing compliance with federal requirements. The single audit process is important for effective oversight but can be modified to be a more timely and effective audit and oversight tool for the Recovery Act and OMB is weighing options on how to modify it.

Nearly half of the estimated spending programs in the Recovery Act will be administered by non-federal entities. State officials suggested opportunities to improve communication in several areas. For example, they wish to be notified when Recovery Act funds are made available directly to prime recipients within their state that are not state agencies.

#### Plans to Evaluate Impact

Two of the several objectives of the Recovery Act are to (1) preserve existing jobs and stimulate job creation and (2) promote economic recovery. Officials in nine of the 16 states and the District expressed concern about determining jobs created and retained under the Recovery Act, as well as methodologies that can be used for estimation of each.

#### GAO's Recommendations

OMB has moved out quickly to guide implementation of the Recovery Act. As OMB's initiatives move forward, it has opportunities to build upon its efforts to date by addressing several important issues.

#### Accountability and Transparency Requirements

The Director of OMB should:

- adjust the single audit process to provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010

- continue efforts to identify methodologies that can be used to determine jobs created and retained from projects funded by the Recovery Act.

- evaluate current requirements to determine whether sufficient, reliable and timely information is being collected before adding further data collection requirements.

#### Administrative Support and Oversight

The Director of OMB should clarify what Recovery Act funds can be used to support state efforts to ensure accountability and oversight.

#### Communications

The Director of OMB should provide timely and efficient notification to (1) prime recipients in states and localities when funds are made available for their use, (2) states, where the state is not the primary recipient of funds, but has a state-wide interest in this information, and (3) all recipients, on planned releases of federal agency guidance and whether additional guidance or modifications are expected.

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United States Government Accountability Office  
Washington, DC 20548

April 23, 2009

Report to Congressional Committees:

The Nation faces what is generally reported to be the most serious economic crisis since the Great Depression. In response, the American Recovery and Reinvestment Act of 2009 (Recovery Act)<sup>1</sup> was enacted to promote economic recovery, make investments, and to minimize and avoid reductions in state and local government services. The Congressional Budget Office (CBO) estimated that the Recovery Act's combined spending and tax provisions will cost \$787 billion over ten years, of which more than \$580 billion will be in additional federal spending. The stated purposes of the Recovery Act are to:

- preserve and create jobs and promote economic recovery;
- assist those most impacted by the recession;
- provide investments needed to increase economic efficiency by spurring technological advances in science and health;
- invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits; and
- stabilize state and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

The Recovery Act specifies several roles for GAO including conducting bimonthly reviews of selected states' and localities' use of funds made available under the act.<sup>2</sup> Accordingly, our objectives for this report were to describe (1) selected states' and localities' uses of and planning for Recovery Act funds, (2) the approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of the Recovery Act funds they received.

To address these objectives, we selected a core group of 16 states and the District of Columbia (District) that we will follow over the next few years to provide an ongoing longitudinal analysis of the use of funds provided in conjunction with the Recovery Act. The states are Arizona, California, Colorado, Florida, Georgia, Iowa, Illinois, Massachusetts, Michigan,

<sup>1</sup>Pub. L. No. 111-5, 123 Stat. 115 (February 17, 2009).

<sup>2</sup>Recovery Act, div. A, title IX, §901.

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Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas. These states contain about 65 percent of the U.S. population and are estimated to receive collectively about two-thirds of the intergovernmental federal assistance funds available through the Recovery Act. We selected these states and the District on the basis of outlay projections, percentage of the U.S. population represented, unemployment rates and changes, and a mix of states' poverty levels, geographic coverage, and representation of both urban and rural areas. In addition, we visited a non-probability sample of about 60 localities within the 16 selected states.<sup>9</sup>

We collected documents from and conducted semi-structured interviews with executive-level state and local officials and staff from Governors' offices, "Recovery Czars," State Auditors, Controllers, and Treasurers. We also interviewed staff from state legislatures. In addition, our work focused on federal, state, and local agencies administering programs receiving Recovery Act funds. We analyzed data and interviewed officials from the federal Office of Management and Budget (OMB). We also analyzed other federal guidance on programs selected for this review and spoke with relevant program officials at the Centers for Medicare & Medicaid Services (CMS), the U.S. Department of Transportation and the U.S. Department of Education. We did not review state legal materials for this report, but relied on state officials and other state sources for description and interpretation of relevant state constitutions, statutes, legislative proposals, and other state legal materials.

We based our selection of the programs to review for this initial report on Recovery Act funding and potential risks associated with receipt of additional funds for these programs. An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways. These three programs are therefore highlighted throughout this report. The information obtained from this review cannot be generalized to all states and localities receiving Recovery Act funding. A detailed description of our scope and methodology can be found in Appendix I.

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<sup>9</sup>This total includes two entities in the District of Columbia which received direct federal funding that was not passed through the District government.

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We conducted this performance audit from February 17, to April 20, 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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## Background

Recovery Act funds are being distributed to states, localities, other entities, and individuals through a combination of formula and competitive grants and direct assistance. Nearly half of the approximately \$580 billion associated with Recovery Act spending programs will flow to states and localities affecting about 50 state formula and discretionary grants as well as about 15 entitlement and other countercyclical programs. As noted above, three of the largest streams of funds flowing to states and localities are (1) the temporary increase in FMAP funding which will provide states with approximately \$87 billion in assistance; (2) the State Fiscal Stabilization Fund, which will provide nearly \$54 billion to help state and local governments avert budget cuts, primarily in education; and (3) highway infrastructure investment funds of approximately \$27 billion.

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## Medicaid FMAP

Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the FMAP. Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states.

Under the Recovery Act, states are eligible for an increased FMAP for expenditures that states make in providing services to their Medicaid populations.<sup>4</sup> The Recovery Act provides eligible states with this increased FMAP for 27 months between October 1, 2008, and December 31, 2010. On

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<sup>4</sup>See Recovery Act, div. B, title V, § 5001 (a)-(c). U.S. territories are also eligible for an increased FMAP subject to a different formula than states. Recovery Act div. B, title V, § 5001 (d).

February 25, 2009, CMS made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>5</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for: (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. For the first two quarters of 2009, the increases in the FMAP for the 16 states and the District ranged from 7.09 percentage points in Iowa to 11.59 percentage points in California. (See table 1.)

**Table 1: FMAP Changes from Fiscal Year 2008 to the First Two Quarters of Fiscal Year 2009, for 16 states and the District**

State	Fiscal Year 2008 FMAP	Fiscal Year 2009 FMAP, first two quarters	Difference
Arizona	66.20	75.01	8.81
California	50.00	61.59	11.59
Colorado	50.00	58.78	8.78
District of Columbia	70.00	77.68	7.68
Florida	56.83	67.64	10.81
Georgia	63.10	73.44	10.34
Illinois	50.00	60.48	10.48
Iowa	61.73	68.82	7.09
Massachusetts	50.00	58.78	8.78
Michigan	58.10	69.58	11.48
Mississippi	76.29	83.62	7.33
New Jersey	50.00	58.78	8.78
New York	50.00	58.78	8.78
North Carolina	64.05	73.55	9.50
Ohio	60.79	70.25	9.46
Pennsylvania	54.08	63.05	8.97
Texas	60.56	68.76	8.20

Source: GAO analysis of HHS data, as of April 16, 2009.

<sup>5</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for Medicaid service expenditures made on or after October 1, 2008.

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**Highway Infrastructure Investment**

The Recovery Act provides approximately \$48 billion to fund grants to states, localities, regional authorities and others for transportation projects of which the largest piece is \$27.5 billion for highway and related infrastructure investments. The Recovery Act largely provides for increased transportation funding through existing programs such as the Federal-Aid Highway Surface Transportation Program—a federally funded, state-administered program. Under this program, funds are apportioned annually to each state department of transportation (or equivalent) to construct and maintain roadways and bridges on the federal-aid highway system. The Federal-Aid Highway Program refers to the separately funded grant programs mostly funded by formula, administered by the Federal Highway Administration (FHWA) in the U.S. Department of Transportation.

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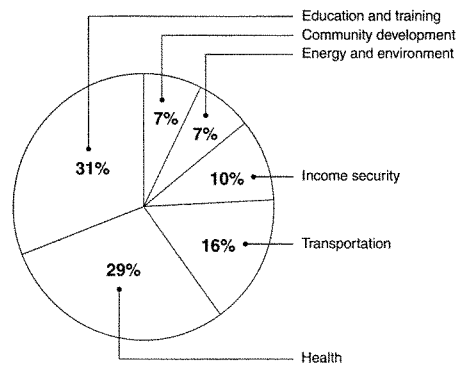
**State Fiscal Stabilization Fund**

The Recovery Act provided \$53.6 billion in appropriations for the State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education. The Recovery Act requires that the Secretary of Education set aside \$5 billion for State Incentive Grants, referred to by the department as the Reach for the Top program, and the establishment of an Innovation Fund. After reserving these and certain other funds, the remaining funds are to be distributed to states by formula, with 61 percent of the state award based on the state's relative share of the population aged 5 to 24 and 39 percent based on the state's relative share of the total U.S. population. The Recovery Act specifies that 81.8 percent (about \$39.5 billion) of these remaining funds are to be distributed to states for support of elementary, secondary, and postsecondary education, and early childhood education programs. The remaining 18.2 percent of SFSF (about \$8.8 billion) is available for public safety and other government services including for educational purposes. The Department of Education announced on April 1, 2009 that it will award the SFSF in two phases. The first phase—\$32.6 billion—represents about two-thirds of the SFSF.

Figure 1 shows the distribution of Recovery Act funds to states by broad functional categories over the next several years.



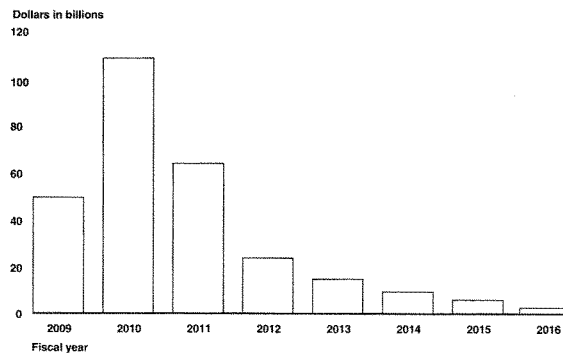
**Figure 1: State and Local Recovery Act Funding by Broad Functional Category, Fiscal Years 2009-2019**



Source: GAO analysis of CBO and FFIS data.

The timeline of Recovery Act spending has been a key issue in the debate and design of the Recovery Act because of the elapsed time between when policy changes are first proposed and actual spending begins to flow from enacted changes. Figure 2 shows the projected timing of state and local-administered Recovery Act spending.

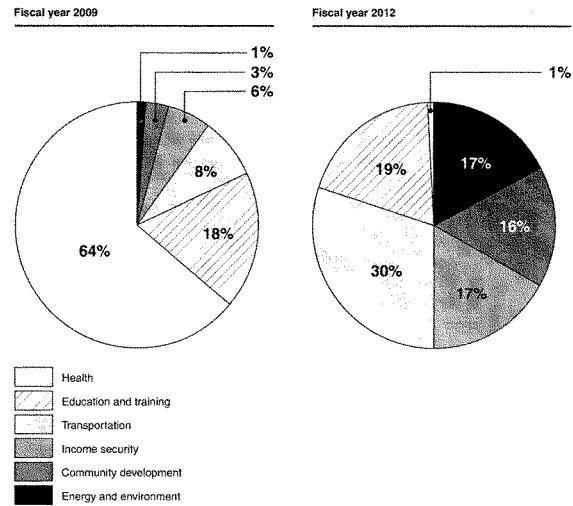
**Figure 2: Projected Timing of Federal Recovery Act Funding Made Available to States and Localities by Fiscal Year**



Source: GAO analysis of CBO and FFIS data.

Over time, the programmatic focus of Recovery Act spending will change. As shown in figure 3, about two-thirds of Recovery Act funds expected to be spent by states in the current 2009 fiscal year will be health related, primarily temporary increases in Medicaid FMAP funding. Health, education, and transportation is estimated to account for approximately 90 percent of fiscal year 2009 Recovery Act funding for states and localities. However, by fiscal year 2012, transportation will be the largest share of state and local Recovery Act funding. Taken together, transportation spending, along with investments in the community development, energy, and environmental areas that are geared more toward creating long-run economic growth opportunities will represent approximately two-thirds of state and local Recovery Act funding in 2012.

**Figure 3: Composition of State and Local Recovery Act Funding, Fiscal Years 2009 and 2012**



Source: GAO analysis of CBO and FFIS data.

The administration has stipulated that every taxpayer dollar spent on economic recovery must be subject to unprecedented levels of transparency and accountability. To that end, the Recovery Act established the Recovery Accountability and Transparency Board to coordinate and conduct oversight of funds distributed under the Act in order to prevent fraud, waste and abuse. The Board includes a Chairman appointed by the President, and ten Inspectors General specified by the

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Act.<sup>6</sup> The Board has a series of functions and powers to assist it in the mission of providing oversight and promoting transparency regarding expenditure of funds at all levels of government. The Board will report on the use of Recovery Act funds and may also make recommendations to agencies on measures to avoid problems and prevent fraud, waste and abuse.

The Board is also charged under the Act with establishing and maintaining a web site, [www.recovery.gov](http://www.recovery.gov), (Recovery.gov) to foster greater accountability and transparency in the use of covered funds. The website currently includes overview information about the Recovery Act, a timeline for implementation, a frequently asked questions page, and an announcement page that is to be regularly updated. The administration plans to develop the site to encompass information about available funding, distribution of funds, and major recipients. The website is required to include plans from federal agencies; information on federal awards of formula grants and awards of competitive grants; and information on federal allocations for mandatory and other entitlement programs by state, county, or other appropriate geographical unit.<sup>7</sup> Eventually, prime recipients of Recovery Act funding will provide information on how they are using their federal funds. Currently, Recovery.gov features projections for how, when, and where the funds will be spent, as well as which states and sectors of the economy are due to receive what proportion of the funds. As money starts to flow, additional data will become available. In addition to Recovery.gov, OMB has also issued guidance directing executive branch agencies to develop a dedicated portion of their web sites for information related to the recovery.

To ensure a high level of accountability, OMB has issued guidance to the heads of federal departments and agencies for implementing and

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<sup>6</sup>The Recovery Accountability and Transparency Board is comprised of a chairperson appointed by the President; Inspectors General from the Departments of Agriculture, Commerce, Education, Energy, Health and Human Services, Homeland Security, Justice, Transportation, Treasury, and the Treasury Inspector General for Tax Administration; and any other Inspector General designated by the President from any agency that expends or obligates Recovery Act funds.

<sup>7</sup>Recovery Act, div. A, title XV, § 1527(c)(11)–(13).

managing activities enacted under the Recovery Act.<sup>8</sup> OMB has also issued for comment detailed reporting requirements for Recovery Act fund recipients that include the number of jobs created and jobs retained as a result of Recovery Act funding.<sup>9</sup> OMB's guidance documents are available on [Recovery.gov](http://Recovery.gov). In addition, the Civilian Acquisition Council and the Defense Acquisition Regulations Council have issued an interim rule revising the Federal Acquisition Regulation (FAR) to require a contract clause that implements these reporting requirements for contracts funded with Recovery Act dollars.<sup>10</sup>

The Recovery Act also assigns GAO a range of responsibilities to help promote accountability and transparency. Some are recurring requirements such as providing bimonthly reviews of the use of funds made available under Division A of the Recovery Act by selected states and localities and reviews of quarterly reports on job creation and job retention as reported by Recovery Act fund recipients. Other requirements include targeted studies in several areas such as small business lending, education, and trade adjustment assistance. We completed the first of these mandates on April 3, 2009, by announcing the appointment of 13 members to the Health Information Technology Policy Committee, a new advisory body established by the Recovery Act. The committee will make recommendations on creating a policy framework for the development and adoption of a nationwide health information technology infrastructure, including standards for the exchange of patient medical information. On April 16, 2009, we issued a report completing a second mandate to report on the actions of the Small Business Administration (SBA) to, among other things, increase liquidity in the secondary market for SBA loans.<sup>11</sup>

<sup>8</sup>See, OMB memoranda, M-09-10, *Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, February 18, 2009, and M-09-15, *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, April 3, 2009.

<sup>9</sup>OMB, "Information Collection Activities: Proposed Collection; Comment Request," 74 *Fed. Reg.* 14824 (Apr. 1, 2009).

<sup>10</sup>74 *Fed. Reg.* 14,639 (March 31, 2009).

<sup>11</sup>GAO, *Small Business Administration's Implementation of Administrative Provisions in the American Recovery and Reinvestment Act of 2009*, GAO-09-507R (Washington, D.C.: April 16, 2009).

### States' and Localities' Use of and Plans for Recovery Act Funds Focus on Purposes of the Act and States' Fiscal Stresses

Officials in the 16 selected states and the District indicated they have used certain Recovery Act funds and continue planning for the use of additional funds they have not yet received. States' existing intergovernmental programs—such as Medicaid, transportation, and education—have been among the first programs to receive Recovery Act funds. Planning continues for the use of Recovery Act funds for these and other program areas. States' planning actions include appointing Recovery Czars; establishing task forces and other entities, and developing public web sites to solicit input and publicize selected projects. In some cases, according to state officials, state legislation will be required to receive and expend funds or to make required changes to programs for eligibility prior to using the funds. States' approaches to planning for Recovery Act funds also vary in response to state legislative and budget processes regarding the use of federal funds and states' fiscal situations.

### States' Use of Recovery Act Funds by Selected Program Areas

The three largest programs making funds available to the state and localities so far have been the Medicaid FMAP, highways funds, and the SFSP. Table 2 shows the breakout of funding available for these three programs in the 16 selected states and the District that GAO visited. Recovery Act funding for these 17 jurisdictions accounts for a little less than two-thirds of total Recovery Act funding for these three programs.

**Table 2: Notification of Recovery Act Funds for GAO Core States and the District of Columbia for Select Programs (Dollars in thousands)**

(Dollars in thousands)			
State	Medicaid FMAP	Highways	States Fiscal Stabilization Fund
Arizona	\$534,576	\$521,958	\$681,360
California	\$3,331,167	\$2,569,568	\$3,993,379
Colorado	\$226,959	\$403,924	\$509,363
District of Columbia	\$87,831	\$123,508	\$59,883
Florida	\$1,394,945	\$1,346,735	\$1,809,196
Georgia	\$521,251	\$931,586	\$1,032,684
Illinois	\$992,042	\$935,593	\$1,376,965
Iowa	\$136,023	\$358,162	\$316,467
Massachusetts	\$1,182,968	\$437,865	\$666,153
Michigan	\$700,522	\$847,205	\$1,066,733
Mississippi	\$225,471	\$354,564	\$321,131
New Jersey	\$549,847	\$651,774	\$891,424
New York	\$3,143,641	\$1,120,685	\$2,021,924

(Dollars in thousands)			
State	Medicaid FMAP	Highways	States Fiscal Stabilization Fund
North Carolina	\$657,111	\$735,527	\$951,704
Ohio	\$760,647	\$935,677	\$1,198,882
Pennsylvania	\$1,043,920	\$1,026,429	\$1,276,766
Texas	\$1,448,824	\$2,250,015	\$2,662,203
<b>Total Case Study</b>	<b>\$16,937,745</b>	<b>\$15,550,776</b>	<b>\$20,836,218</b>
<b>Percent of National Total</b>	<b>70</b>	<b>58</b>	<b>64</b>
<b>National Total</b>	<b>\$24,233,145</b>	<b>\$26,660,000</b>	<b>\$32,552,620</b>
<b>Notifications as of</b>	<b>April 3, 2009</b>	<b>March 2, 2009</b>	<b>April 2, 2009</b>

Source: GAO analysis of agency data.

Note: For Medicaid FMAP amounts shown are the increased Medicaid FMAP Grant Awards as of April 3, 2009. For Highways, the amounts shown are the full state apportionment. For the SFSPF, the amounts shown are the initial release of the state allocation.

#### Medicaid FMAP

Under the Recovery Act, states are eligible for an increased FMAP for expenditures that states make in providing services to their Medicaid populations.<sup>12</sup> The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008 and December 31, 2010. Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for: (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates.

In our sample of 16 states and the District, officials from 15 states and the District indicated that they had drawn down increased FMAP grant awards, totaling \$7.96 billion for the period of October 1, 2008 through April 1, 2009—47 percent of their increased FMAP grant awards. In our sample, the extent to which individual states and the District accessed these funds varied widely, ranging from 0 percent in Colorado to about 66 percent in New Jersey. Nationally, the 50 states and several territories combined have drawn down approximately \$11 billion as of April 1, 2009,

<sup>12</sup>See Recovery Act, div. B, title V, § 5001 (a)-(c). U.S. territories are also eligible for an increased FMAP subject to a different formula than states. Recovery Act div. B, title V, § 5001 (d).

which represents almost 46 percent of the increased FMAP grants awarded for the first three quarters of federal fiscal year 2009 (Table 3).<sup>13</sup>

**Table 3: FMAP Grant Awards and Funds Drawn Down, for 16 States and the District**

(Dollars in thousands)

State	FMAP grant awards	Funds drawn	Percentage of funds drawn
Arizona	\$534,576	\$286,286	53.6
California	\$3,331,167	\$1,511,539	45.4
Colorado	\$226,959	0	0.0
District of Columbia	\$87,831	\$49,898	56.8
Florida	\$1,394,945	\$817,025	58.6
Georgia	\$521,251	\$311,515	59.8
Illinois	\$992,042	\$117,081	11.8
Iowa	\$136,023	\$81,663	60.0
Massachusetts	\$1,182,968	\$272,559	23.0
Michigan	\$700,522	\$462,982	66.1
Mississippi	\$225,471	\$114,112	50.6
New Jersey	\$ 549,847	\$362,235	65.9
New York	\$3,143,641	\$1,739,073	55.3
North Carolina	\$657,111	\$414,644	63.1
Ohio	\$760,647	\$420,630	55.3
Pennsylvania	\$1,043,920	\$330,811	31.7
Texas	\$1,448,824	\$665,665	45.9
<b>Total</b>	<b>\$16,937,745</b>	<b>\$7,957,718</b>	<b>47.0</b>

Source: GAO analysis of HRIS data.

Note: FMAP grant awards are those funds awarded as of April 3, 2009, and funds drawn down are as of April 1, 2009.

In order for states to qualify for the increased FMAP available under the Recovery Act, they must meet certain requirements. In particular

- **Maintenance of Eligibility:** In order to qualify for the increased FMAP, states generally may not apply eligibility standards, methodologies, or procedures that are more restrictive than those in effect under their state Medicaid programs on July 1, 2008.<sup>14</sup> In

<sup>13</sup>This amount includes funds drawn down by U.S. territories and the District.

<sup>14</sup>See Recovery Act, div. B, title V, § 5001(f)(1).



guidance to states, CMS noted that examples of restrictions of eligibility could include (1) the elimination of any eligibility groups since July 1, 2008 or (2) changes in an eligibility determination or redetermination process that is more stringent than what was in effect on July 1, 2008. States that fail to initially satisfy the maintenance of eligibility requirements have an opportunity to reinstate their eligibility standards, methodologies, and procedures before July 1, 2009 and become retroactively eligible for the increased FMAP.

- **Compliance with Prompt Payment:** Under federal law states are required to pay claims from health practitioners promptly.<sup>15</sup> Under the Recovery Act, states are prohibited from receiving the increased FMAP for days during any period in which that state has failed to meet this requirement.<sup>16</sup> Although the increased FMAP is not available for any claims received from a practitioner on each day the state is not in compliance with these prompt payment requirements, the state may receive the regular FMAP for practitioner claims received on days of non-compliance. CMS officials told us that states must attest that they are in compliance with the prompt payment requirement, but that enforcement is complicated due to differences across states in methods used to track this information. CMS officials plan to issue guidance on reporting compliance with the prompt payment requirement and are currently gathering information from states on the methods they use to determine compliance.
- **Rainy Day Funds:** States are not eligible for an increased FMAP if any amounts attributable (either directly or indirectly) to the increased FMAP are deposited or credited into any reserve or rainy day fund of the state.<sup>17</sup>
- **Percentage Contributions from Political Subdivisions:** In some states, political subdivisions—such as cities and counties—may be required to help finance the state's share of Medicaid spending. States that have such financing arrangements are not eligible to receive the

<sup>15</sup>States are required to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt. See 42 U.S.C. § 1396a(a)(37)(A).

<sup>16</sup>This provision only applies to claims received after February 17, 2009, the date of enactment of the Recovery Act.

<sup>17</sup>This prohibition does not apply to any increase in FMAP based on maintenance of the states' prior year FMAPs.

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increased FMAP if the percentage contributions required to be made by a political subdivision are greater than what was in place on September 30, 2008.<sup>19</sup>

In addition to meeting the above requirements, states that receive the increased FMAP must submit a report to CMS no later than September 30, 2011 that describes how the increased FMAP funds were expended, in a form and manner determined by CMS.<sup>19</sup> In guidance to states, CMS has stated that further guidance will be developed for this reporting requirement. CMS guidance to states also indicates that, for federal reimbursement, increased FMAP funds must be drawn down separately, tracked separately, and reported to CMS separately. Officials from several states told us they require additional guidance from CMS on tracking receipt of increased FMAP funds and on reporting on the use of these funds.

The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services.<sup>20</sup> However, the receipt of this increased FMAP may reduce the state share for their Medicaid programs. States have reported using these available funds for a variety of purposes. In our sample, individual states and the District reported that they would use the funds to maintain their current level of Medicaid eligibility and benefits, cover their increased Medicaid caseloads—which are primarily populations that are sensitive to economic downturns, including children and families, and to offset their state general fund deficits thereby avoiding layoffs and other measures detrimental to economic recovery. Ten states and the District reported using these funds to maintain program eligibility. Nine states and the District reported using these funds to maintain benefits. Specifically, Massachusetts reported that during a previous financial downturn, the state limited the number of individuals eligible for some services and reduced certain program benefits that were optional for the state to cover. However, with the funds made available as a result of the increased FMAP, the state did not have to make such reductions. Similarly, New Jersey reported that the state used these funds to eliminate premiums for certain children in its State Children's Health Insurance

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<sup>19</sup>This prohibition does not apply to any increase in FMAP based on maintenance of the states' prior year FMAPs.

<sup>19</sup>Recovery Act, div. B, title V, § 5001 (g)(1).

<sup>20</sup>Recovery Act, div. B, title V, § 5001 (a)-(c), (h)(1).

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Program, allowing it to retain coverage for children whose enrollment in the program would otherwise have been terminated for non-payment of premiums. Nine states and the District reported using these funds to cover increases to their Medicaid caseloads, primarily to populations that are sensitive to economic downturns, such as children and families. For example, New Jersey indicated that these funds would help the state meet the increased demand for Medicaid services. According to a New Jersey official, due to significant job losses, the state's proposed 2010 budget would not have accommodated all the applicants newly eligible for Medicaid and that the funds available as a result of the increased FMAP have allowed the state to maintain a "safety net" of coverage for uninsured and unemployed people. In addition, 10 states and the District indicated that the increased funds made available would help offset deficits in their general funds. Pennsylvania reported that because funding for its Medicaid program is derived, in part, on state revenues, program funding levels fluctuate as the economy rises and falls. However, the state was able to use funds made available to offset the effects of lower state revenues. Arizona officials also reported that the state used funds made available as a result of the increased FMAP to pay down some of its debt and make payroll payments, thus allowing the state to avoid a serious cash flow problem.

Finally, six states in our sample also reported that they used funds made available as a result of the increased FMAP to comply with prompt payment requirements. Specifically, Illinois reported that these funds will permit the state to move from a 90-day payment cycle to a 30-day payment cycle for all Medicaid providers. Three states also reported using these funds to restore or to increase provider payment rates.

In our sample, many states and the District indicated that they need additional guidance from CMS regarding eligibility for the increased FMAP funds. Specifically, 5 states raised concerns about whether certain programmatic changes could jeopardize the state's eligibility for these funds. For example Texas officials indicated that guidance from CMS is needed regarding whether certain programmatic changes being considered by Texas, such as a possible extension of the program's eligibility period, would affect the state's eligibility for increased FMAP funds. Similarly, Massachusetts wanted clarification from CMS as to whether certain changes in the timeframe for the state to conduct eligibility re-determinations would be considered a more restrictive standard. Four states also reported that they wanted additional guidance from CMS regarding policies related to the prompt payment requirements or changes to the non-federal share of Medicaid expenditures. For example, California

officials noted that the state reduced Medicaid payments for in-home support services, but that counties could voluntarily choose to increase these payments without altering the cost sharing arrangements between the counties and the state. The state wants clarification from CMS on whether such an arrangement would be allowable in light of the Recovery Act requirements regarding the percentage of contributions by political subdivisions within a state toward the non-federal share of expenditures.

In response to states' concerns regarding the need for guidance, CMS told us that it is in the process of developing draft guidance on the prompt payment provisions in the Recovery Act. One official noted that this guidance will include defining the term practitioner, describing the types of claims applicable under the provision, and addressing the principles that are integral to determining a state's compliance with prompt payment requirements. Additionally, CMS plans to have a reporting mechanism in place through which states would report compliance under this provision. With regard to Recovery Act requirements regarding political subdivisions, CMS described their current activities for providing guidance to states. Due to the variability of state operations, funding processes, and political structures, CMS has been working with states on a case-by-case basis to discuss particular issues associated with this provision and to address the particular circumstances for each state. A CMS official told us that if there were an issue(s) or circumstance(s) that had applicability across the states, or if there were broader themes having national significance, CMS would consider issuing guidance.

#### Highway Infrastructure Investment

Of the \$27.5 billion provided in the Recovery Act for highway and related infrastructure investments, \$26.7 billion is provided to the 50 states for restoration, repair, construction and other activities allowed under the Federal-Aid Highway Surface Transportation Program and for other eligible surface transportation projects. Nearly one-third of these funds are required to be sub-allocated to metropolitan and other areas. States must follow the requirements for the existing program, and in addition, the Recovery Act requires that the Governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. The certifications must include a statement of the amount of funds the state planned to expend from state sources as of the date of enactment, during the period beginning on the date of enactment through September 30, 2010, for the types of projects that are funded by the appropriation.

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The U.S. Department of Transportation is reviewing the Governors' certifications regarding maintaining their level of effort for highways. According to the Department, of the 16 states in our review and the District of Columbia, three states have submitted a certification free of explanatory or conditional language—Arizona, Michigan, and New York. Eight submitted “explanatory” certifications—certifications that used language that articulated assumptions used or stated the certification was based on the “best information available at the time,” but did not clearly qualify the expected maintenance of effort on the assumptions proving true or information not changing in the future. Six submitted a “conditional” certifications, which means that the certification was subject to conditions or assumptions, future legislative action, future revenues, or other conditions.<sup>21</sup>

Recovery Act funding for highway infrastructure investment differs from the usual practice in the Federal-aid Highway Program in a few important ways. Most significantly, for projects funded under the Recovery Act, the federal share is 100 percent; typically projects require a state match of 20 percent while the federal share is typically 80 percent. Under the Recovery Act, priority is also to be given to projects that are projected to be completed within three years. In addition, within 120 days after the apportionment by the Department of Transportation to the states (March 2, 2009), and specifically before June 30, 2009, 50 percent of the apportioned funds must be obligated.<sup>22</sup> Any amount of this 50 percent of apportioned funding that is not obligated may be withdrawn by the Secretary of Transportation and redistributed to other states that have obligated their funds in a timely manner. Furthermore, one year after enactment the Secretary will withdraw any remaining unobligated funds and redistribute them based on states' need and ability to obligate additional funds. These provisions are applicable only to those funds apportioned to the state and not those funds required by the Recovery Act to be suballocated to metropolitan, regional and local organizations.

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<sup>21</sup>The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>22</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

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Finally, states are required to give priority to projects that are located in economically distressed areas as defined by the Public Works and Economic Development Act of 1965, as amended. In March 2009, FHWA directed its field offices to provide oversight and take appropriate action to ensure that states gave adequate consideration to economically distressed areas in selecting projects. Specifically, field offices were directed to discuss this issue with the states and to document its review and oversight of this process.

States are undertaking planning activities to identify projects, obtain approval at the state and federal level and move them to contracting and implementation. However, because of the steps necessary before implementation, states generally had not yet expended significant amounts of Recovery Act funds. States are required to reach agreement with the Department of Transportation (DOT) on a list of projects reimbursement from DOT for these projects. States will then request reimbursement from DOT as the state makes payments to contractors working on approved projects.

As of April 16, 2009, the U.S Department of Transportation reported that nationally \$6.4 billion of the \$26.6 billion in Recovery Act highway infrastructure investment funding provided to the states had been obligated – meaning Transportation and the states had reached agreements on projects worth this amount. As shown in Table 4 below, for the locations that GAO reviewed, the extent to which the Department of Transportation had obligated funds apportioned to the states and Washington D.C. ranged from 0 to 65 percent. For two of the states, the Department of Transportation had obligated over 50 percent of the states' apportioned funds, for 4 it had obligated 30 to 50 percent of the states' funds, for 9 states it had obligated under 30 percent of funds, and for three it had not obligated any funds.

Table 4: Highway Apportionments and Obligations as of April 16, 2009 (Dollars in millions)

State	Amount apportioned	Amount obligated	Percent of apportionment obligated	Number of projects
Arizona	\$522	\$148	28	26
California	2,570	261	10	20
Colorado	404	118	29	19
District of Columbia	124	37	30	1
Florida	1,347	0	0	0
Georgia	932	0	0	0
Illinois	936	606	65	214
Iowa	358	221	62	107
Massachusetts	425	64	15	19
Michigan	847	111	13	27
Mississippi	355	137	39	32
New Jersey	652	281	43	12
New York	1,121	277	25	108
North Carolina	736	165	22	53
Ohio	936	0	0	0
Pennsylvania	1,026	309	30	108
Texas	2,250	534	24	159
<b>Total</b>	<b>\$15,538</b>	<b>\$3,269</b>	<b>21</b>	<b>905</b>

Source: FHWA.

Note: Totals may not add due to rounding.

In most states we visited, while they had not yet expended significant funds, they were planning to solicit bids in April or May. They also stated that they planned to meet statutory deadlines for obligating the highway funds. A few states had already executed contracts. As of April 1, 2009, the Mississippi Department of Transportation (MDOT), for example, had signed contracts for 10 projects totaling approximately \$77 million.<sup>23</sup> These projects include the expansion of State Route 19 in eastern Mississippi into a four-lane highway. This project fulfills part of MDOT's 1987 Four-Lane Highway Program which seeks to link every Mississippian to a four-lane highway within 30 miles or 30 minutes. Similarly, as of April 15, 2009, the Iowa Department of Transportation had competitively awarded 25 contracts valued at \$168 million. Most often, however, we found that

<sup>23</sup> As of April 16, 2009, the U.S. Department of Transportation had obligated \$137.0 million for 32 Mississippi projects.

highway funds in the states and the District have not yet been spent because highway projects were at earlier stages of planning, approval, and competitive contracting. For example, in Florida, the Department of Transportation (FDOT) plans to use the Recovery Act funds to accelerate road construction programs in its preexisting 5-year plan which will result in some projects being reprioritized and selected for earlier completion. On April 15, 2009, the Florida Legislative Budget Commission approved the Recovery Act-funded projects that FDOT had submitted.

For the most part, states were focusing their selection of Recovery Act-funded highway projects on construction and maintenance, rather than planning and design, because they were seeking projects that would have employment impacts and could be implemented quickly. These included road repairs and resurfacing, bridge repairs and maintenance, safety improvements, and road widening. For example, in Illinois, the Department of Transportation is planning to spend a large share of its estimated \$655 million in Recovery Act funds<sup>24</sup> for highway and bridge construction and maintenance projects in economically distressed areas, those that are shovel-ready, and those that can be completed by February 2012. In Iowa, the contracts awarded have been for projects such as bridge replacements and highway resurfacing—shovel-ready projects that could be initiated and completed quickly. Knowing that the Recovery Act would include opportunities for highway investment, states told us they worked in advance of the legislation to identify appropriate projects. For example, in New York, the state DOT began planning to manage anticipated federal stimulus money in November 2008. A key part of New York's DOT's strategy was to build on existing planning and program systems to distribute and manage the funds.

#### State Fiscal Stabilization Fund

The states and D.C. must apply to the Department of Education for SFSSF funds. Education will award funds once it determines that an application contains key assurances and information on how the state will use the funds. As of April 20, applications from three states had met that determination—South Dakota, and two of GAO's sample states, California

<sup>24</sup>According to the Federal Highway Administration, Illinois' share of Recovery Act funds for highway infrastructure investment is approximately \$936 million. This total consists of \$655 million for IDOT projects and \$281 million in sub-allocations for local governments' highway projects. The \$655 million to IDOT includes \$627 million for IDOT to use statewide and \$28 million for mandatory transportation enhancements. Transportation enhancements include activities such as provision of facilities for pedestrians and bicyclists, preservation of abandoned railway corridors, acquisition of scenic easements, and historic preservation projects.



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and Illinois. The applications from other states are being developed and submitted and have not yet been awarded. The states and the District report that SFSF funds will be used to hire and retain teachers, reduce the potential for layoffs, cover budget shortfalls, and restore funding cuts to programs. The applications to Education must contain certain assurances. For example, states must assure that, in each of fiscal years 2009, 2010, and 2011, they will maintain state support at fiscal year 2006 levels for elementary and secondary education and also for public institutions of higher education (IHEs). However, the Secretary of Education may waive maintenance of effort requirements if the state demonstrates that it will commit an equal or greater percentage of state revenues to education than in the previous applicable year. The state application must also contain (1) assurances that the state is committed to advancing education reform in increasing teacher effectiveness, establishing state-wide education longitudinal data systems, and improving the quality of state academic standards and assessments; (2) baseline data that demonstrates the state's current status in each of the education reform areas; and (3) a description of how the state intends to use its stabilization allocation.

Within two weeks of receipt of an approvable SFSF application, Education will provide the state with 67 percent of its SFSF allocation. Under certain circumstances, Education will provide the state with up to 90 percent of its allocation. In the second phase, Education intends to conduct a full peer review of state applications before awarding the final allocations.

After maintaining state support for education at fiscal year 2006 levels, states are required to use the education portion of the SFSF to restore state support to the greater of fiscal year 2008 or 2009 levels for elementary and secondary education, public IHEs, and, if applicable, early childhood education programs. States must distribute these funds to school districts using the primary state education formula but maintain discretion in how funds are allocated to public IHEs. If, after restoring state support for education, additional funds remain, the state must allocate those funds to school districts according to the funding formula found in Title I, Part A, of the Elementary and Secondary Education Act of 1965 (ESEA), commonly known as the No Child Left Behind Act. However, if a state's education stabilization fund allocation is insufficient to restore state support for education, then a state must allocate funds in proportion to the relative shortfall in state support to public schools and IHEs. Education stabilization funds must be allocated to school districts and public IHEs and cannot be retained at the state level.

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Once stabilization funds are awarded to school districts and public IHEs, they have considerable flexibility over how they use those funds. School districts are allowed to use stabilization funds for any allowable purpose under the Elementary and Secondary Education Act (ESEA), (commonly known as the No Child Left Behind Act), the Individuals with Disabilities Education Act (IDEA), the Adult Education and Family Literacy Act, or the Perkins Act, subject to some prohibitions on using funds for, among other things, sports facilities and vehicles. In particular, because allowable uses under the Impact Aid provisions of ESEA are broad, school districts have discretion to use Recovery Act funding for things ranging from salaries of teachers, administrators, and support staff to purchases of textbooks, computers, and other equipment. The Recovery Act allows public IHEs to use SFSF funds in such a way as to mitigate the need to raise tuition and fees, as well as for the modernization, renovation, and repair of facilities, subject to certain limitations. However, the Recovery Act prohibits public IHEs from using stabilization funds for such things as increasing endowments, modernizing, renovating, or repairing sports facilities, or maintaining equipment. According to Education officials, there are no maintenance of effort requirements placed on local school districts. Consequently, as long as local districts use stabilization funds for allowable purposes, they are free to reduce spending on education from local-source funds, such as property tax revenues.

States have broad discretion over how the \$8.8 billion in SFSF funds designated for basic government services are used. The Recovery Act provides that these funds can be used for public safety and other government services and that these services may include assistance for education, as well as for modernization, renovation, and repairs of public schools or IHEs, subject to certain requirements. Education's guidance provides that the funds can also be used to cover state administrative expenses related to the Recovery Act. However, the Act also places several restrictions on the use of these funds. For example, these funds cannot be used to pay for casinos (a general prohibition that applies to all Recovery Act funds), financial assistance for students to attend private schools, or construction, modernization, renovation, or repair of stadiums or other sports facilities.

States' expected that SFSF uses by school districts and public IHEs would include retaining current staff and spending on programmatic initiatives, among other uses. Some states' fiscal condition could affect their ability to meet maintenance of effort (MOE) requirements in order to receive SFSF monies, but they are awaiting final guidance from Education on procedures to obtain relief from these requirements. For example, due to

substantial revenue shortages, Florida has cut their state budget in recent years and the state will not be able to meet the maintenance-of-effort requirement to readily qualify for these funds. The state will apply to Education for a waiver from this requirement; however, they are awaiting final instructions from Education on submission of the waiver. Florida plans to use SFSF funds to reduce the impact of any further cuts that may be needed in the state education budget.

In Arizona, generally, state officials expect that SFSF recipients, such as local school districts, will use their allocations to improve the tools they use to assess student performance and determine to what extent performance meets federal academic standards, rehire teachers that were let go because of prior budget cuts, retain teachers, and meet the federal requirement that all schools have equal access to highly qualified teachers, among other things. Funds for the state universities will help them maintain services and staff as well as avoid tuition increases. Illinois officials stated that the state plans to use all of the \$2 billion in State Fiscal Stabilization funds, including the 18.2 percent allowed for government services, for K-12 and higher education activities and hopes to avert layoffs and other cutbacks many districts and public colleges and universities are facing in their fiscal year 2009 and 2010 budgets. State Board of Education officials also noted that U.S. Department of Education guidance allows school districts to use stabilization funds for education reforms, such as prolonging school days and school years, where possible. However, officials said that Illinois districts will focus these funds on filling budget gaps rather than implementing projects that will require long-term resource commitments. While planning is underway, most of the selected states reported that they have not yet fully decided how to use the 18.2 percent of the SFSF which is discretionary.

Localities Report Limited Initial  
Use of Recovery Act Funds

In addition to funds for Medicaid, transportation, and SFSF which flow primarily directly to the states, the Recovery Act provided funds for other program areas ranging from housing to training to alternative energy. Localities' planning for the use of Recovery Act education funds varied according to both the status of federal guidance in place at the time of our review and individuals states' and localities' own planning process. New Jersey state education officials said they were initially limited in their ability to provide guidance to local institutions because they were awaiting guidance from the U.S. Department of Education. As a result, school district officials we interviewed in Newark and Trenton said they are waiting for state officials to tell them what their allocations are for each of the federal Recovery Act education programs. The timing of the federal and state guidelines for these funds are important as the local schools

districts are planning their upcoming fiscal year budgets and would like to know how the Recovery Act funds would complement their upcoming school spending. According to the governor's chief of staff, the state already funds local school districts with \$8.8 billion in state funds, so ensuring accountability for the use of state funds to so many school districts is not a new challenge to the state oversight agencies. On April 1, 2009, the U.S. Department of Education issued guidance to the states on how Recovery Act funds could be used for education. State officials are continuing to review the guidance, and on April 16, 2009, issued guidance to local school districts outlining each district's allocation of additional funds made available under the Recovery Act for programs authorized under Title I of the Elementary and Secondary Education Act (ESEA) and the Individuals with Disabilities Education Act. In Arizona, Tempe School District No. 3 plans to use the vast majority of the Recovery Act funding for ESEA Title I for existing programs, but it has tentative plans to use portions of it each year to hire two temporary regional facilitators and to fund five existing preschool programs, among other uses.

Officials from the selected states and the District said there were plans in place to apply for and use Recovery Act funds. For example, Michigan plans to apply for \$67 million in Recovery Act funds for crime control and prevention activities under the Department of Justice's Edward Byrne Memorial Justice Assistance Grants. Michigan Department of Community Health officials told us that about \$41 million of these funds will support, among other things, state efforts to reduce the crime lab backlog, funding for multi-jurisdictional courts, and localities' efforts regarding law enforcement programs, community policing, and local correctional resources. An additional \$26 million in Recovery Act funds will go directly to localities to support efforts against drug-related and violent crime. On April 13, 2009, Michigan began accepting grant applications for the Byrne program and will continue to accept them until May 11, 2009. In another example, officials in the District told us that as of April 3, 2009, the District Department of Employment Services had received about \$1.5 million for adult Workforce Investment Act (WIA) programs, about \$3.8 million for dislocated workers programs, and almost \$4 million for youth programs. They said that D.C. plans to use these Recovery Act funds in accordance with the U.S. Department of Labor's guidance stating the intent of the Recovery Act to use WIA Adult funds to provide the necessary services to substantially increased numbers of adults to support their entry or reentry into the job market, and that WIA Dislocated Worker funds be used to provide the necessary services to dislocated workers to support their reentry into the job market.

**Recovery Act Funds  
Expected to Alleviate  
Some State Fiscal  
Pressures As States  
Continue to Adjust Budget  
Plans to Address Current  
and Emerging Challenges**

Officials in all of the selected states indicated they were able to reduce or eliminate expected budget shortfalls through the inclusion of Recovery Act funds in their budget projections. In Texas, some representatives told us that absent the availability of Recovery Act funds, state agencies likely would have been asked to make cuts of about 10 percent for the state's fiscal year 2010-2011 biennial budget, in addition to the state drawing upon the rainy day fund. However, other officials representing the Texas Office of the Governor said that budget deficit situations do not necessarily result in the state using its rainy day fund. The officials stressed that—to meet the requirement to pass a balanced budget—a variety of other solutions could be considered, such as budget reallocations among state agencies and programs, as well as spending cuts. Colorado officials said Recovery Act funds will help prevent cuts to state programs such as transportation. Illinois officials said the state hopes to avert layoffs and create new jobs with Recovery Act funds.

Officials in Massachusetts also said that federal Recovery Act funds are critical to addressing the Commonwealth's immediate fiscal pressures. State officials expect to use a significant portion of funds made available as a result of their state-projected \$8.7 billion in Recovery Act funds (over 2 years) for budget stabilization. As of April 2009, the Commonwealth is addressing a budget shortfall of approximately \$3.0 billion, driven largely by lower-than-anticipated revenues. The combination of funds made available as a result of the increased FMAP and state rainy day funds—a reserve fund built up during more favorable economic conditions to be used during difficult economic times—will help the state avoid cuts in several areas, including health care, education, and public safety. Faced with declining revenue projections since fiscal year 2008, Pennsylvania officials believe that funds made available as a result of the Recovery Act are critical to help alleviate the immediate fiscal pressure and help balance the state budget. Based on February 2009 projections, Pennsylvania faces a \$2.3 billion shortfall in fiscal year 2009, largely because of lower-than-expected revenues.

Despite the infusion of Recovery Act funds into state budgets, some state officials reported that the current fiscal situation still requires action to maintain balanced budgets. These actions include budget reductions, fee increases and scaling back of state rebates of local property taxes. In Georgia, officials amended the state budget by reducing revenue estimates, using reserves, and cutting program funding. These actions were necessary despite the inclusion of additional Medicaid funds made available as a result of the Recovery Act. The largest budget cuts in New Jersey come from scaling back of state rebates of local property taxes by

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\$500 million, and reducing state payments to the pension funds by \$895 million.

Officials in the selected states acknowledged the Recovery Act's contributions to easing immediate fiscal pressures but remain wary of continued fiscal pressures likely to remain after federal assistance ends. Officials in several states reported that their planning efforts focused on maintaining existing services rather than creating new programs or staff positions which could extend their state's financial liabilities beyond the end date for Recovery Act funds. Officials generally expected to use Recovery Act funds to fill gaps in existing programs rather than funding new initiatives. In the midst of program budget cuts, state officials acknowledged the challenge of ensuring that, where required to do so, they use Recovery Act funds to supplement and not supplant current state program funds.<sup>25</sup> For example, in Arizona, programs receiving Recovery Act funds may have a share of the state general fund reduced to help balance the fiscal year 2010 budget, thus demonstrating the state has met the prohibition on supplanting state funds could be a challenge. The Arizona Treasurer's Office estimated that even with Recovery Act funding, Arizona's expenditures were expected to exceed revenues through about 2014, and the state's "rainy day" fund has been depleted.<sup>26</sup>

In California, even when the state Legislative Analyst's Office factors in the state's anticipated Recovery Act funding and a package of state budget solutions that will be voted on in a May 19, 2009 special election, it estimates an \$8 billion deficit in fiscal year 2009-10. Further, since the release of the governor's budget in January 2009, the state's economic condition continues to deteriorate, and the state legislature and governor may need to develop additional budgetary solutions to rebalance the 2009-10 budget following an update of the budget in May.<sup>27</sup>

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<sup>25</sup>For certain programs, states may use Recovery Act funds to supplement but may not supplant current state program funds. Certain other programs are not subject to this restriction.

<sup>26</sup>In addition, the Arizona state legislature passed a budget in January 2009 that closed an estimated shortfall of \$1.8 billion for fiscal year 2008 and \$2.1 billion for fiscal year 2009.

<sup>27</sup>In January 2009, the fiscal year 2009-2010 Governor's Budget projected that the state would end the 2009-2010 period with a \$41.6 billion deficit if the state took no corrective actions.

**States' Actions to Plan for Use of Recovery Act Funds Include New and Existing Entities and Processes**

All of the 16 selected states and the District reported taking action to plan for and monitor the use of Recovery Act funding. Some states reported that Recovery Act planning activities for funds received by the state are directed primarily by the governor's office. In New York, for example, the governor provides program direction to the state's departments and offices, and he established a Recovery Act Cabinet comprised of representatives from all state agencies and many state authorities to coordinate and manage Recovery Act funding throughout the state. In North Carolina, Recovery Act planning efforts are led by the newly created Office of Economic Recovery and Investment, which was established by the governor to oversee the state's economic recovery initiatives.

Other states reported that their Recovery Act planning efforts were less centralized. In Mississippi, the governor has little influence over the state Departments of Education and Transportation, as they are led by independent entities. In Texas, oversight of federal Recovery Act funds involves various stakeholders, including the Office of the Governor, the Office of the Comptroller of Public Accounts, and the State Auditor's Office as well as two entities established within the Texas legislature specifically for this purpose—the House Select Committee on Federal Economic Stabilization Funding and the House Appropriations' Subcommittee on Stimulus.<sup>28</sup>

Several states reported that they have appointed "Recovery Czars" or identified a similar key official and established special offices, task forces or other entities to oversee the planning and monitor the use of Recovery Act funds within their states. In Michigan, the governor appointed a recovery czar to lead a new Michigan Economic Recovery Office, which is responsible for coordinating Recovery Act programs across all state departments and with external stakeholders such as GAO, the federal OMB, and others.

Some states began planning efforts before Congress passed the Recovery Act. For example, the state of Georgia recognized the importance of accounting for and monitoring Recovery Act funds and directed state agencies to take a number of steps to safeguard Recovery Act funds and

<sup>28</sup>Under Texas law, according to state officials, the governor is the state's chief budget officer, but the state legislature and the Legislative Budget Board have a large role in the state's budget process, which operates on a 2-year cycle. Both the governor and the Legislative Budget Board develop budget recommendations and submit budget proposals to the legislature, which adopts a budget (general appropriations bill) for the 2-year period.

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mitigate identified risks. Georgia established a small core team in December 2008 to begin planning for the state's implementation of the Recovery Act. Within 1 day of enactment, the governor appointed a Recovery Act Accountability Officer, and she formed a Recovery Act implementation team shortly thereafter. The implementation team includes a senior management team, officials from 31 state agencies, an accountability and transparency support group comprised of officials from the state's budget, accounting, and procurement offices, and five cross-agency implementation teams. At one of the first implementation team meetings, the Recovery Act Accountability Officer disseminated an implementation manual to agencies, which included multiple types of guidance on how to use and account for Recovery Act funds, and new and updated guidance is disseminated at the weekly implementation team meetings.

In contrast, officials in some states are using existing mechanisms rather than creating new offices or positions to lead Recovery Act efforts. For example, a District official stated that the District would not appoint a Recovery Czar, and instead would use its existing administrative structures to distribute and monitor Recovery Act funds to ensure quick disbursement of funds. In Mississippi, officials from the Governor's Office said that the state did not establish a new office to provide statewide oversight of Recovery Act funding, in part because they did not believe that the act provided states with funds for administrative expenses—including additional staff. The Governor did designate a member of his staff to act as a stimulus coordinator for Recovery Act activities.

All 16 states we visited and the District have established Recovery Act web sites to provide information on state plans for using Recovery funding, uses of funds to date, and, in some instances, to allow citizens to submit project proposals. For example, Ohio has created [www.recovery.Ohio.gov](http://www.recovery.Ohio.gov), which represents the state's efforts to create an open, transparent, and equitable process for using Recovery Act funds. The state has encouraged citizens to submit proposals for use of Recovery Act funds, and as of April 8, 2009, individuals and organizations from across Ohio submitted more than 23,000 proposals. Iowa officials indicated they want to use the state's recovery web site ([www.recovery.Iowa.gov](http://www.recovery.Iowa.gov)) to host a "dashboard" function to report updated information on Recovery Act spending that is easily searchable by the public. Also in Colorado, the state plans to create a web-based map of projects receiving Recovery Act funds to help inform the public about the results of Recovery Act spending in Colorado.



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#### States' Legislatures Approve Use of Recovery Act Funds

In many states we spoke to, officials reported that their planning efforts were affected by the need for the state legislature to approve state agencies' use of Recovery Act funds.<sup>29</sup> For example, in Florida, the state legislature must authorize the use of all Recovery Act funds received by the state; including those passed on to local governments. In Colorado, some Recovery Act funds, including those going to Child Care Development Block Grants (CDBG) and the Temporary Assistance to Needy Families (TANF) Emergency Contingency Fund, must be allocated by the Colorado General Assembly, which is in session only through early May. Mississippi officials also plan to use Recovery Act funds to address the state's fiscal challenges. Mississippi legislative officials we met with told us that the state legislature was considering adding escalation language to the current fiscal year's appropriations bills that would authorize state agencies to spend any Recovery Act funds received. The legislature normally conducts its regular session between the beginning of January and the end of March. However, the legislature recessed early during the 2009 regular session in part because of uncertainty regarding how Recovery Act funds that the state will receive should be spent. The legislature plans to reconvene in early May 2009 to complete its work on the state's fiscal year 2010 budget.

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#### Selected States' and the District's Plans to Track Recovery Act Funds

The selected states' and localities' tracking and accounting systems are critical to the proper execution and accurate and timely recording of transactions associated with the Recovery Act. OMB has issued guidance to the states and localities that provides for separate "tagging" of Recovery Act funds so that specific reports can be created and transactions can be traced. Officials from all 16 of the selected states and the District told us they have established or were establishing methods and processes to separately identify (i.e., tag), monitor, track, and report on the use of the Recovery Act funds they receive. The states and localities generally plan on using their current accounting system for recording Recovery Act funds, but many are adding identifiers to account codes to track recovery act funds separately. Many said this involved adding digits to the end of existing accounting codes for federal programs. In California for instance, officials told us that while their plans for tracking, control, and oversight are still evolving, they intend to rely on existing accountability

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<sup>29</sup>We did not review state legal materials for this report, but relied on state officials and other state sources for description and interpretation of relevant state constitutions, statutes, legislative proposals, and other state legal materials.

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mechanisms and accounting systems, enhanced with newly created codes, to separately track and monitor Recovery Act funds that are received by and pass through the state. Several officials told us that the state's accounting system should be able to track Recovery Act funds separately.

In one state, Arizona, officials told us that state agencies will primarily be responsible for administering, tracking, reporting on and overseeing Recovery Act funds for their respective programs because the state government is highly decentralized. The state's existing accounting system will have new accounting codes added in order to segregate and track the Recovery Act funds separately from other funds that will flow through the state government. Under Arizona's decentralized government, some larger agencies, and program offices within them, have their own accounting systems that will need to code and track Recovery Act funds as well. The Arizona General Accounting Office has issued guidance to state agencies on their responsibilities, including how they were to receive, disburse, tag or code in their accounting systems, track separately, and to some extent report on these federal resources.

A concern expressed by state officials is that agencies within the state often use different accounting software making it difficult to ensure consistent and timely reporting. For example, Georgia officials stated that the majority of state agencies use the same software; however, some agencies do not use this software and others have greatly customized the software. Similarly, officials from the Illinois Office of the Internal Auditor said that the state is assessing an issue that could affect reporting — specifically that there are currently more than 100 separate financial systems used throughout the Illinois state government. Furthermore, Colorado state officials are concerned that their accounting system is outdated and said they faced challenges in meeting federal reporting requirements. Some state departments do not use the state financial system grant module and therefore manually post aggregate revenue and expenditure data. As a result, they may have to compile a list of Recovery Act funding received outside of their central financial management system. State officials are determining what approach they will use in tracking funds, and told us they plan to create an accounting fund and a centrally defined budget coding structure through which to track state agencies' use of Recovery Act funds.

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**State Concerns Over Accountability of Recovery Act Funds Going to Sub-Recipients or Directly to Localities and Other Non-State Entities**

State officials reported a range of concerns regarding the federal requirements to identify and track Recovery Act funds going to sub-recipients, localities and other non-state entities. These concerns include their inability to track these funds with existing systems, uncertainty regarding state officials' accountability for the use of funds which do not pass through state government entities, and their desire for additional federal guidance to establish specific expectations on sub-recipient reporting requirements.

Officials from many of the 16 selected states and the District told us that they had concerns about the ability of sub-recipients, localities, and other non-state entities to separately tag, monitor, track, and report on the Recovery Act funds they receive. For example, in New Jersey officials noted that certain towns and cities, as well as regional planning organizations, can apply for and directly receive federal funds under the terms of the Recovery Act. According to the state Inspector General, the risk for waste, fraud and abuse increases the farther removed an organization is from state government controls. While some state officials said that they have statewide investigative authority, they would not be able to readily track the funding going directly to local and regional government organizations and nonprofits as a result of the funding delivery and reporting requirements set up in the Recovery Act. In addition, staff from the State Auditor's office noted that some smaller cities and towns in New Jersey are not used to implementing guidance from the state or federal government on how they are using program funds and this could result in the localities reporting using funds for ineligible purposes.

Officials in many states expressed concern about being held accountable for funds flowing directly from federal agencies to localities or other recipients. For example, officials in Colorado expressed concern that they will be held accountable for all Recovery Act funds flowing to the state, including those funds for which they do not have oversight or even information about, because some funds flow directly to non-state entities within Colorado (such as school districts and transportation districts).

Officials in some states said they would like to at least be informed about funds provided to non-state entities in order to facilitate planning for the use of these funds and so they can coordinate Recovery Act activities. For example, Georgia officials do not expect to track and report on funds going directly to localities, but would like to be informed about these funds so that the state can coordinate with localities. They cited Recovery Act-funded broadband initiatives and health funding to nonprofit hospitals

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as areas where a lack of coordination could result in a duplication of services or missed opportunities to leverage resources. Officials at the Colorado Department of Public Safety told us that, because Colorado and other states expressed interest in receiving data on localities' grant funding, the federal Bureau of Justice Assistance in the U.S. Department of Justice began providing data to the states on localities' funding.

In another example, officials told us that the Ohio Administrative Knowledge System (OAKS) will allow the state to tag Recovery Act funding. However, they said in many cases state agencies will rely on grantees and contractors to track the funds to their end use. Because the state intends to code each Recovery Act funding stream separately and recipients typically manage more than one funding stream at a time, state officials said recipients should be able to track Recovery Act funds separately from other funding sources. However, state and local officials we interviewed raised concerns about the capacity of grantees and contractors to track funds spent by sub-recipients. For example, officials with the Ohio Department of Education said they can track Recovery Act funds to school districts and charter schools, but they have to rely on the recipients' financial systems to be able to track funds beyond that. An official with the Columbus City Schools said that while they could provide assurances that Recovery Act funds were spent in accordance with program rules; they could not report back systematically how each federal Recovery Act dollar was spent. Officials with the Columbus Metropolitan Housing Authority also noted limitations in how far they could reasonably be expected to track Recovery Act funds. They said they could track Recovery Act dollars to specific projects but could not systematically track funds spent by subcontractors on materials and labor. These officials added, however, that if they required the contractors to collect this information from their subcontractors, they would be able to report back with great detail. Still, they said, without additional guidance from the federal government on specific reporting requirements, they were hesitant to specify requirements for their contractors to collect the data.

Pennsylvania officials said that the state will rely on sub-recipients to meet reporting requirements at the local level. Recipients and sub-recipients can be local governments or other entities such as transit agencies. For example, about \$367 million in Recovery Act money for transit capital assistance and fixed guideway (such as commuter rails and trolleys) modernization was allocated directly to areas such as Philadelphia, Pittsburgh, and Allentown. State officials also told us that the state would not track or report Recovery Act funds that go straight from the federal

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government to localities and other entities, such as public housing authorities.

Officials in several states indicated that either their states would not be tracking Recovery Act funds going to the local levels or that they were unsure how much data would be available on the use of these funds. For example, Massachusetts officials told us that the portion of recovery funds going directly to recipients other than Massachusetts state government agencies, such as independent state authorities, local governments, or other entities, will not be tracked through the Office of the Comptroller. While state officials acknowledged that the Commonwealth lacks authority to ensure adequate tracking of these funds, they also are concerned about the ability of smaller entities to manage Recovery Act funds, particularly smaller municipalities that traditionally do not receive federal funds and who are not familiar with Massachusetts tracking and procurement procedures, and recipients receiving significant increases in federal funds. In order to address this concern, the state administration introduced emergency legislation that, according to state officials, includes a provision requiring all entities within Massachusetts that receive Recovery Act money to provide information to the state on their use of Recovery Act funds. Nevertheless, two large non-state government entities we spoke with—the city of Boston and the Massachusetts Bay Transportation Authority (an independent authority responsible for the metropolitan Boston's transit system)—believe that their current systems, with some modifications, will allow them to meet Recovery Act requirements. For example, the city of Boston hosted the Democratic National Convention in 2004 and officials said that their system was then capable of segregating and tracking a sudden influx of temporary funds.

This response was common among the selected states. For example, officials in Florida told us that the state's accounting system will not track the portion of Recovery Act funds that flow directly to local entities from federal agencies. Officials in Michigan's Auditor General's Office told us that their oversight responsibilities do not include most sub-recipients that receive direct federal funding, so any upfront safeguards to track or ensure accountability have not been determined.<sup>30</sup> Mississippi officials also said that although special accounting codes will be added to the Statewide Automated Accounting System in order to track the expenditure

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<sup>30</sup>Some Michigan state departments are sub-recipients of other state departments and so these recipients are under the State Auditor General's authority.

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of Recovery Act funds, the system would not track Recovery Act funds allocated directly to local and regional government organizations and nonprofit organizations.

In Arizona, the portion of recovery funds going directly to recipients other than Arizona government agencies, such as independent state authorities, local governments, or other entities, may not be tracked by the state. State officials expressed concern that they may not be able to attest to localities' ability to tag, track, and report on Recovery Act funds when these entities receive the moneys directly from federal agencies rather than through state agencies. Department heads and program officials generally expected that they could require sub-recipients receiving funds from the state, through agreements, grant applications, and revised contract provisions, to separately track and report Recovery Act funding. For example, unemployment program managers said they were issuing new intergovernmental agreements with localities to cover new reporting requirements. However, several of the state officials did raise questions about the ability of some local organizations to do this, such as small, rural entities, boards or commissions, or private entities not used to doing business with the federal government. Furthermore, several of the state department officials acknowledged that either some state agency information systems have data reliability problems, which will have to be resolved, or they had sub-recipients who in the past had problems providing timely and accurate reporting, but said that they would work with these entities to comply, and also had sanctions to use as a last resort.

Officials in Arizona, Florida, Georgia, and New York, also expressed concern that the new requirement to provide reports on use of Recovery Act funds within 10 days after a quarter ends may be challenging to meet by both state and local entities. In some program areas, some state officials raised concerns that the Recovery Act requirement will create much shorter deadlines for processing financial data that local areas will have difficulty meeting.

### Selected States' and Localities' Internal Controls and Safeguards to Manage and Mitigate the Risk of Mismanagement, Waste, Fraud, and Abuse of Recovery Act Funds

The selected states and the District are taking various approaches to ensure that internal controls are in place to manage risk up-front, rather than after problems develop and deficiencies are identified after the fact, and have different capacities to manage and oversee the use of Recovery Act funds. Many of these differences result from the underlying differences in approaches to governance, organizational structures, and related systems and processes that are unique to each jurisdiction. A robust system of internal control specifically designed to deal with the unique and complex aspects of the Recovery Act funds will be key to helping management of the states and localities achieve the desired results. Effective internal control can be achieved through numerous different approaches, and, in fact, we found significant variation in planned approaches by state. For example,

- New York's Recovery Act cabinet plans to establish a working group on internal controls; the Governor's office plans to hire a consultant to review the state's management infrastructure and capabilities to achieve accountability, effective internal controls, compliance and reliable reporting under the act; and, the state plans to coordinate fraud prevention training sessions.
- Michigan's Recovery Office is developing strategies for effective oversight and tracking of the use of Recovery Act funds to ensure compliance with accountability and transparency requirements.
- Ohio's Office of Internal Audit plans to assess the adequacy and effectiveness of the current internal control framework and test whether state agencies adhere to the framework.
- Florida's Chief Inspector General established an enterprise-wide working group of agency program Inspectors General who are updating their annual work plans by including the Recovery Act funds in their risk assessments and will leave flexibility in their plans to address issues related to funds.
- Massachusetts's Joint Committee on Federal Recovery Act Oversight will hold hearings regarding the oversight of Recovery Act spending.
- Georgia's State Auditor plans to provide internal control training to state agency personnel in late April. The training will discuss basic internal controls, designing and implementing internal controls for Recovery Act programs, best practices in contract monitoring, and reporting on Recovery Act funds.

**States' and Localities' Internal Controls Will Be Critical to Ensuring That Recovery Act Funds Are Used Appropriately**

Internal controls include management and program policies, procedures, and guidance that help ensure effective and efficient use of resources; compliance with laws and regulations; prevention and detection of fraud, waste, and abuse; and the reliability of financial reporting. Because Recovery Act funds are to be distributed as quickly as possible, controls are evolving as various aspects of the program become operational. Effective internal control is a major part of managing any organization to achieve desired outcomes and manage risk. GAO's Standards for Internal Control include five key elements: control environment, risk assessment, control activities, information and communication, and monitoring.<sup>31</sup>

**Control Environment**

The control environment should create a culture of accountability by establishing a positive and supportive attitude toward improvement and the achievement of established program outcomes. Control environment includes the integrity and ethical values maintained and demonstrated by management, the organizational structure, and management's philosophy and operating style. As detailed earlier in this report, although the implementation has varied, many locations we reviewed have attempted to enhance their control environment through the appointment of a Recovery czar or the establishment of boards or working groups that focus on the Recovery Act. Also, as noted earlier, state officials expressed concerns about the reliability and accuracy of data coming from localities.

**Risk Assessments**

The second feature of strong internal controls is risk assessment—that is, performing comprehensive reviews and analyses of program operations to determine if risks exist and the nature and extent of risks have been identified. Some states told us that they are conducting such risk assessments and the existing body of work by state auditors and others provide a good roadmap for states to use to pinpoint key areas of concern and to strengthen internal controls and subsequent oversight. For example, the Illinois Office of Internal Audit is performing a risk assessment of all programs related to the Recovery Act, and North Carolina's Office of Internal Audit is assessing the risk of the state department's financial management system and internal controls. Michigan's major state departments are conducting self assessments of controls, including identification of internal control and programmatic weaknesses. In Georgia, the budget office is requiring state agencies to complete a tool that assesses risk as part of the budget process for the

<sup>31</sup>GAO, *Standards for Internal Control in the Federal Government*, GAO/AIMD-00-21.3.1 (Washington, D.C.: November 1999).



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Recovery Act funds. Selected states have thus far identified various risks that the Recovery Act funds and programs face, including Georgia officials identifying three state departments with increased risk—the Georgia Department of Labor that is on a different accounting system than other state departments, the Georgia Department of Transportation which had previously identified accounting problems and is currently being reorganized, and the Georgia Department of Human Resources, which is currently being divided into three parts, which increases risk. Additionally, Massachusetts’ fiscal year 2007 Single Audit report also identified deficiencies, especially in the Department of Education’s sub-recipient monitoring.

Officials in several of the selected states told us that risk assessment is being conducted to look at programs receiving Recovery Act funds. Officials in Texas’ State Auditor’s Office noted that relatively high risks generally can be anticipated with certain types of programs such as new programs with completely new processes and internal controls; programs that distribute significant amounts of funds to local governments or boards, and programs that rely on sub-recipients for internal controls and monitoring. Officials from New York, North Carolina, and Pennsylvania commented that the weatherization program was an example of a program at increased risk.

The results of recent audits are a readily available source of information to use in the risk assessment process. Material weaknesses and other conditions identified in an audit represent potential risks that can be analyzed for their significance and occurrence that will allow management and others to decide how to manage the risk and what actions should be taken. A readily available source of information on internal control weaknesses and other risks present in the states and other jurisdictions receiving Recovery Act funding is the Single Audit report, prepared to meet the requirements of the Single Audit Act, as amended (Single Audit Act) and OMB’s implementing guidance in OMB Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations. The Single Audit Act adopted a single audit concept to help meet the needs of federal agencies for grantee oversight and accountability as well as grantees’ needs for single, uniformly structured audits. The Single Audit Act requires states, local governments and nonprofit organizations expending over \$500,000 in federal awards in a year to obtain an audit in accordance with

requirements set forth in the Act.<sup>32</sup> A single audit consists of (1) an audit and opinions on the fair presentation of the financial statements and the Schedule of Expenditures of Federal Awards (SEFA); (2) gaining an understanding of and testing internal control over financial reporting and the entity's compliance with laws, regulations, and contract or grant provisions that have a direct and material effect on certain federal programs (i.e., the program requirements);<sup>33</sup> and (3) an audit and an opinion on compliance with applicable program requirements for certain federal programs. The audit report also includes the auditor's schedule of findings and questioned costs, and the auditee's corrective action plans and a summary of prior audit findings that includes planned and completed corrective actions. Auditors are also required to report on significant deficiencies in internal control and on compliance associated with the audit of the financial statements.

For example, in California, the most recent single audit conducted by the State Auditor for fiscal year 2007 identified 81 material weaknesses, 27 of which were associated with programs we reviewed for purposes of this report.<sup>34</sup> The State Auditor plans to use past audit results to target state agencies and programs with a high number and history of problems, including data reliability concerns, and is closely coordinating with us on these efforts. For example, the fiscal year 2007 State Single Audit Report identified 8 material weaknesses pertaining to the ESEA Title I program and the Individuals with Disabilities Education Act programs. The audit findings included a material weakness in the California Department of Education's management of cash because it disbursed funds without assurances from LEAs that the time between the receipt and disbursement of federal funds was minimized, contrary to federal guidelines. Education officials told us that they have addressed some of these material weaknesses and, in other cases, they are still working to correct them. If

<sup>32</sup>If an entity expends federal awards under only one federal program, the entity may elect to have an audit of that program.

<sup>33</sup>The auditor identifies the applicable federal programs, including "major programs," based on risk criteria, including minimum dollar thresholds, set out in the Single Audit Act and OMB Circular No. A-133. Guidance on identifying compliance requirements for most large federal programs is set out in the Compliance Supplement to OMB Circular No. A-133. OMB has 14 requirements that generally are to be tested for each major federal program to opine on compliance and report on significant deficiencies in internal control over compliance with each applicable compliance requirement.

<sup>34</sup>State of California: Internal Control and State and Federal Compliance Audit Report for the Fiscal Year Ended June 30, 2007 (June 2008 Report 2007-002).

these and other material weaknesses are not corrected, they may affect the state's ability to appropriately manage certain Recovery Act funds. The State Auditor's Office told us that it is in the process of finalizing the fiscal year 2007 State Single Audit Report and plans to issue the report within the next 30 days. In addition, the State Auditor's Office is summarizing the results of the single audit to identify those programs that continue to have material weaknesses. Finally, the State Auditor's Office plans to use the results of other audits it has conducted in conjunction with the single audit to develop its approach for determining the state's readiness to receive the large influx of federal funds and comply with the requirement regarding the use of those funds under the Recovery Act.

Arizona's fiscal year 2007 Single Audit report identified a number of material weaknesses related to the state Department of Education. The report identified a material weakness involving IDEA where the state department had not reviewed sub-recipients to ensure that federal awards were used for authorized purposes in compliance with laws, regulations, and the provisions of contracts or grant agreements. The Audit report also identified one financial reporting material weaknesses related to the state Department of Administration's ability to prepare timely financial statements, including its Comprehensive Annual Financial Report (CAFR). In fiscal year 2007, the CAFR was issued in June 2008, approximately 6 months after the scheduled deadline. According to the Auditor General's Office, the fiscal year 2008 CAFR will also be completed late as the last agency submitted its financial statement on March 9, 2008. According to the Auditor General's Office, this control deficiency affects the timeliness of financial reporting which affects the needs of users. It is especially important that Arizona try to address the timeliness issue with regard to financial statements given the number and strict reporting timelines that are imposed on states under the Recovery Act.

#### Control Activities

The third element of a comprehensive system of internal controls is that of control activities, which involve taking actions to address identified risk areas and help ensure that management's decisions, directives, and plans are carried out and program objectives met. Various control activities already exist and are also being put in place in the states related to the Recovery Act. Control activities for states and localities consist of the policies, procedures, and guidance that enforce management's directives and achieve effective internal control over specific program activities. Examples of such policies and procedures particularly relevant to the Recovery Act spending are (1) proper execution and accurate and timely recording of transactions and events, (2) controls to help ensure compliance with program requirements, (3) establishment and review of

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performance measures and indicators, and (4) appropriate documentation of transactions and internal control.

Documented policies, procedures and guidance that are effectively implemented will be critical tools for states and localities management and staff as well as program recipients for achieving good management of Recovery Act programs. Control activities are also key in helping to achieve accurate, reliable reporting of information and results.

Effective control activities and monitoring are key to achieving this objective. Pennsylvania's Auditor General also found potential weaknesses and vulnerabilities in programs expected to receive Recovery Act funds.<sup>36</sup> For example, a recent Auditor General report found, among other things, weak internal controls, weaknesses in contracting, and inconsistent verification and inspection of subcontractor work in the state's Weatherization Assistance Program. States and localities that receive and administer the Recovery Act funds will be expected to minimize fraud, waste, and abuse in contracting.

According to Florida state officials, the state completed an initiative to strengthen contracting requirements several years ago. For example, the majority of state contracts greater than \$1 million are required to be reviewed for certain criteria by the Department of Financial Services' Division of Accounting and Auditing before the first payment is processed. The contract must also be negotiated by a contract manager certified by the Florida Department of Management Services, Division of State Purchasing Training and Certification Program. In another example of efforts to enhancing contracting processes and oversight, officials in New Jersey told us that the controls and reports will be put into place by the state's centralized purchasing department, the Division of Purchase and Property (DPP). The current accounting system will be able to account for and control the use of Recovery Act funds used for procurement because DPP will create special accounting codes for these funds. New Jersey officials stated that their accounting systems had the capability to track funds using special accounting codes and that they were confident no special enhancements were needed to their accounting software, although they would monitor the accounting system to ensure it was functioning

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<sup>36</sup>Other audits the office performs include: financial audits of counties, and state aided and owned institutions; performance audits of state agencies, programs and state owned institutions; financial and compliance audits of school districts; special investigations; and audits of the operations of welfare county assistance offices.

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	<p>properly. DPP will also publicly advertise bids for projects funded with Recovery Act funds, include terms and conditions in each request for proposals and contract for these projects stating detailed reports required by the Act, and will post contract award notices for Recovery Act-funded projects.</p>
Information and Communication	<p>Information should be communicated to management and within the entity to enable accountable officials and others throughout the entity to carry out their responsibilities and determine whether they are meeting their goals of accountability and efficient use of resources. The states have undertaken a variety of information and communication methods. For the Recovery Act, internal state communication is being conducted through newly created task forces or working groups such as those in California and the District, implementation teams such as in Florida and Georgia, and state offices such as in North Carolina. Texas also uses a periodic forum of the internal audit staff of Texas state agencies for another statewide communication method. Various officials are developing guidance related to the Recovery Act and dispensing the information to state agencies.</p>
Monitoring	<p>Monitoring activities include the systemic process of reviewing the effectiveness of the operation of the internal control system. These activities are conducted by management, oversight boards and entities, and internal and external auditors. Monitoring enables stakeholders to determine whether the internal control system continues to operate effectively over time. It also improves the organization's overall effectiveness and efficiency by providing timely evidence of changes that have occurred, or might need to occur, in the way the internal control system addresses evolving or changing risks.</p> <p>Many of the boards or offices discussed in the control environment above have responsibilities related to monitoring the Recovery Act funds. States have undertaken various other activities to monitor Recovery Act funds, including Arizona's budget director meeting with the heads of programs potentially receiving Recovery Act funds to gauge each programs' preparedness; Arizona's Comptroller conducting a survey to inventory current internal controls at state agencies to help ensure controls are in place to limit the risk of fraud, waste, abuse and mismanagement of Recovery Act funds; California's Governor appointing the state's first Inspector General specifically to oversee Recovery Act funds as they are disbursed in the state; Massachusetts' legislature creating the Joint Committee on federal Recovery Act Oversight with the goals of ensuring compliance with federal regulations and reviewing current state laws, regulations and policies to ensure they allow access to Recovery Act funds</p>

and streamline the processes to quickly stimulate the economy; and Texas State Auditor's Office plans to hire 10 additional staff.

An important aspect of monitoring Recovery Act funding includes sub-recipient monitoring. As noted, significant concerns exist regarding sub-recipient monitoring, as this is an area where limited experience and known vulnerabilities exist. Some state auditors do not have authority to monitor local operations of internal controls. For example, in Pennsylvania, officials from the Auditor General's office have different views about what authority they have to audit federal money that flows directly to localities, such as housing authorities and municipalities.

In Texas, the State Auditor's Office made a recommendation regarding the monitoring of sub-recipients in its most recent audit of the Texas Education Agency.<sup>36</sup> The audit report did not find that sub-recipients were improperly spending federal funds or were not meeting federal requirements, however the report did note that the agency had "a limited number of resources available to monitor fiscal compliance." The audit report recommended that the Texas Education Agency continue to add resources, within its budget constraints, to increase the amount of federal fiscal compliance performed. According to the State Auditor, following the audit in February 2009, the Texas Education Agency created a comprehensive correction plan to address this resource issue, which the agency is implementing.

**Current Single Audit Focus  
May Not Provide Timely  
Oversight Information for  
Recovery Act Funds**

OMB's Circular No. A-133 sets out implementing guidelines for the single audit and defines roles and responsibilities related to the implementation of the Single Audit Act, including detailed instructions to auditors on how to determine which federal programs are to be audited for compliance with program requirements in a particular year at a given grantee. The Circular No. A-133 Compliance Supplement is issued annually to guide auditors on what program requirements should be tested for programs audited as part of the single audit. OMB has stated that it will use its Circular No. A-133 Compliance Supplement to notify auditors of program requirements that should be tested for Recovery Act programs, and will issue interim updates as necessary.

<sup>36</sup>State Auditor's Office, *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2008*, SAO Report No. 09-330 (Austin, Tex., Feb. 2009). The audit was performed by an independent public auditing firm under contract to the State Auditor's Office.

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Both the Single Audit Act and OMB Circular No. A-133 call for a “risk-based” approach to determine which programs will be audited for compliance with program requirements as part of a single audit. In general, the prescribed approach relies heavily on the amount of federal expenditures during a fiscal year and whether findings were reported in the previous period to determine whether detailed compliance testing is required for a given program that year.<sup>37</sup> Under the current approach for risk determination in accordance with Circular No. A-133, certain risks unique to the Recovery Act programs may not receive full consideration. Recovery Act funding carries with it some unique challenges. The most significant of these challenges are associated with (1) new government programs (2), the sudden increase in funds or programs that are new for the recipient entity, and (3) the expectation that some programs and projects will be delivered faster so as to inject funds into the economy. This makes timely and efficient evaluations in response to the Recovery Act’s accountability requirements critical. Specifically,

- new programs and recipients participating in a program for the first time may not have the management controls and accounting systems in place to help ensure that funds are distributed and used in accordance with program regulations and objectives;
- Recovery Act funding that applies to programs already in operation may cause total funding to exceed the capacity of management controls and accounting systems that have been effective in past years;
- the more extensive accountability and transparency requirements for Recovery Act funds will require the implementation of new controls and procedures; and
- risk may be increased due to the pressures of spending funds quickly.

In response to the risks associated with Recovery Act funding, the single audit process needs adjustment to put appropriate focus on Recovery Act programs to provide the necessary level of accountability over these funds in a timely manner. The single audit process could be adjusted to require the auditor to perform procedures such as the following as part of the routine single audit:

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<sup>37</sup>The Single Audit Act requires that all major programs be audited and specifies minimum dollar amounts and minimum proportions of federal funds expended for programs to be identified by the auditor as major programs. See 31 U.S.C. §§ 7501.

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- provide for review of the design and implementation of internal control over compliance and financial reporting for programs under the Recovery Act;
  - consider risks related to Recovery Act-related programs in determining which federal programs are major programs; and
  - specifically, test Recovery Act programs to determine whether the auditee complied with laws and regulations.<sup>38</sup>

The first two items above should preferably be accomplished during 2009 before significant expenditures of funds in 2010 so that the design of internal control can be strengthened prior to the majority of those expenditures. We further believe that OMB Circular No. A-133 and/or the Circular No. A-133 Compliance Supplement could be adjusted to provide some relief on current audit requirements for low-risk programs to offset additional workload demands associated with Recovery Act funds.

OMB told us that it is developing audit guidance that would address the above audit objectives. OMB also said that it is considering reevaluating potential options for providing relief from certain existing audit requirements in order to provide some balance to the increased requirements for Recovery Act program auditing.

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#### State and Local Capacity to Manage Risks

Officials in several states expressed concerns regarding the lack of funding provided to state oversight entities in the Recovery Act given the additional federal requirements placed on states to provide proper accounting, and ensure transparency. Due to fiscal constraints, many states reported significant declines in the number of management and oversight staff—limiting states' ability to ensure proper implementation and management of Recovery Act funds. To the extent that states' management infrastructures were already strained due to resource issues, risks will be exacerbated by increased workloads and new program implementation. While the majority of states indicated that they lack the necessary resources to conduct additional management and oversight related to the Recovery Act, some states indicated that they are taking

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<sup>38</sup>The Single Audit Act sets out minimum federal expenditure amounts and proportions to use as criteria in defining which programs are to be tested for compliance with program requirements during a single audit. OMB will need to consider those statutory criteria when considering revisions to the single audit process.



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measures to either hire new staff or reallocate existing staff to ensure adequate oversight of Recovery Act funds.

Officials we interviewed in several states said the lack of funding for state oversight entities in the Recovery Act presents them with a challenge, given the increased need for oversight and accountability. According to state officials, state budget and staffing cuts have limited the ability of state and local oversight entities to ensure adequate management and implementation of the Recovery Act. For example, Colorado's state auditor reported that state oversight capacity is limited, noting that the Department of Health Care Policy and Financing has had 3 controllers in the past 4 years and the state legislature's Joint Budget Committee recently cut field audit staff for the Department of Human Services in half. In addition, the Colorado Department of Transportation's deputy controller position is vacant, as is the Department of Personnel & Administration's internal auditor position. Colorado officials noted that these actions are, in part, due to administrative cuts during a past economic downturn in an attempt to maintain program delivery levels.

In Massachusetts, the task forces the Governor convened in December 2008 concluded that it is critical the Inspector General and State Auditor have resources to audit Recovery Act contracts and management of Recovery Act funds, as well as recommended that the Attorney General's office be provided with the resources to promptly and effectively pursue fraud and abuse. Massachusetts officials explained that the oversight community is facing budget cuts of about 10 percent at a time when increased oversight and accountability is critically needed. To illustrate the impact of the impending budget situation, the Inspector General stated that his department does not have the resources to conduct any additional oversight related to Recovery Act funds. This significantly affects the Inspector General's capacity to conduct oversight since the budget is almost entirely comprised of salaries, and any cuts in funding would result in fewer staff available to conduct oversight. In addition, the Massachusetts State Auditor described how their department has had to resort to staff being furloughed already for 6 days and is anticipating further layoffs before the end of fiscal year 2009. Similarly, 94 percent of their department's budget is labor and any cuts in funding generally result in cuts in staff. Much like Colorado and Massachusetts, Arizona and Florida state officials report significant declines in oversight staff. The Florida Auditor General told us that the office has not been hiring new staff for over a year and has about 10 percent of the office's positions unfilled. In addition, the Office of Policy Analysis and Government Accountability officials also told us their respective staffs have decreased

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by 10 percent in the past two years. State officials stated that these staff resource constraints may lead them to reassess priorities and reallocate staff to ensure adequate oversight of Recovery Act funds.

Officials within Arizona state executive offices that are coordinating oversight activities—such as the Office of Strategic Planning and Budgeting, the Office of Economic Recovery, and the Comptroller's Office—stated that they will need additional people to help ensure compliance with Recovery Act funding requirements, but that the state has a hiring freeze to help address budget deficits. For example, the General Accounting Office within the state Department of Administration has experienced a reduction from 74 to 50 staff, posing challenges to its increased oversight responsibilities, and the state Department of Economic Security that manages workforce investment programs had 8,214 staff on furloughs of five or nine days, depending on pay grade, and has laid off about 800 staff members as well. Similarly, a state Department of Housing official stated that the office currently has a vacancy rate of about 15 percent because of the hiring freeze. Furthermore, the state Auditor General reported that its staffing levels are nearly 25 percent below the authorized staffing level of 229 full time equivalents.

Although most states indicated that they lack the resources needed to provide effective monitoring and oversight, some states indicated they will hire additional staff to help ensure the prudent use of Recovery Act funds. For example, according to officials with North Carolina's Governor's Crime Commission, the current management capacity in place is not sufficient to implement the Recovery Act. Officials explained that the Recovery Act funds for the Edward Byrne Memorial Justice Assistance Grant program have created an increase in workload that the department will have to hire additional staff to handle over the next 3 years. Officials explained that these staff will be hired for the short term since the money will run out in 3 years. Additionally, officials explained that they are able to use 10 percent of the Justice Assistance Grants funding to pay for the administrative positions that are needed.

In addition, officials from Ohio's Office of Budget and Management (OBM) stated that its Office of Internal Audit plans to increase its internal audit staff from 9 (current) to 33 by transferring internal audit personnel from other state agencies and hiring new staff by July 2009. OBM officials say that the increase in Office of Internal Audit staff will provide the needed resources to implement its objectives and ensure that current safeguards are in place and followed as the state manages its Recovery Act funded programs. Additionally, some Georgia state officials that directly

Hiring Freezes May Limit Some  
States' Capacity to Provide  
Effective Management and  
Oversight

administer programs stated that overseeing the influx of funds could be a challenge, given the state's current budget constraints and hiring freeze. For example, the State Auditor, whose fiscal year 2009 budget was cut by 11 percent, expressed concerns about the lack of additional funds for Recovery Act oversight. The Georgia State Auditor noted that, if state fiscal conditions do not improve or federal funding does not become available for audit purposes, additional budget and staffing cuts may occur within the department. In some cases, state officials told us that they planned to use Recovery Act funds to cover their administrative costs. Meanwhile, other state officials want additional clarity on when they could use program funds to cover such costs.

A number of states expressed concerns regarding the ability to track Recovery Act funds due to state hiring freezes, resulting from budget shortfalls. For instance, New Jersey has not increased its number of state auditors or investigators, nor has there been an increase in funding specifically for Recovery Act oversight. In addition, the state hiring freeze has not allowed many state agencies to increase their Recovery Act oversight efforts. For example, despite an increase of \$469 million in Recovery Act funds for state highway projects, no additional staff will be hired to help with those tasks or those directly associated with the Recovery Act, such as reporting on the number of jobs created. While the state's Department of Transportation has committed to shift resources to meet any expanded need for internal Recovery Act oversight, one person is currently responsible for reviewing contractor-reported payroll information for disadvantaged business enterprises, ensuring compliance with Davis-Bacon wage requirements, and development of the job creation figures. State education officials in North Carolina also said that greater oversight capacity is needed to manage the increase in federal funding. However, due to the state's hiring freeze, the agency will be unable to use state funds to hire the additional staff needed to oversee Recovery Act funds. The North Carolina Recovery Czar said that his office will work with state agencies to authorize hiring additional staff when directly related to Recovery Act oversight.

Michigan officials reported that the state's hiring freeze may not allow state and local agencies to hire the additional staff needed to increase Recovery Act oversight efforts. For example, an official with the state's Department of Community Health said that because it has been downsizing for several years through attrition and early retirement, it does not have sufficient staff to cover its current responsibilities and that further reductions are planned for fiscal year 2010. However, state officials told us that they will take the actions necessary to ensure that state

	<p>departments have the capacity to provide proper oversight and accountability for Recovery Act funds.</p> <p>In contrast, two states indicated that they have or will have sufficient levels of existing personnel to track funds. Texas state officials noted that state agencies plan on using existing staff to manage the stimulus funds. Agency officials will monitor the situations and, as need arises, will determine whether additional staff should be hired to ensure adequate oversight of the state Recovery Act funds. Additionally, in preparation of the infusion of Recovery Act funds, the Illinois Governor is seeking approximately 350 additional positions state-wide in the fiscal year 2010 budget to help implement Recovery Act programs, according to officials from the Governor's Office of Management and Budget.</p>
Local Oversight Capacity	<p>With respect to oversight of Recovery Act funding at the local level, varying degrees of preparedness were reported by state and local officials. While the California Department of Transportation (Caltrans) officials stated that extensive internal controls exist at the state level, there may be control weaknesses at the local level. Caltrans is collaborating with local entities to identify and address these weaknesses. Likewise, Colorado officials expressed concerns that effective oversight of funds provided to Jefferson County may be limited due to the recent termination of its internal auditor and the elimination of its internal control audit function. Arizona state officials expressed some concerns about the ability of rural, tribal, and some private entities such as; boards, commissions, and nonprofit organizations to manage, especially if the Recovery Act does not provide administrative funding for some programs.</p>
<b>State Plans to Assess Recovery Act Spending Impact</b>	<p>As recipients of Recovery Act funds and as partners with the federal government in achieving Recovery Act goals, states and local units of government are expected to invest Recovery Act funds with a high level of transparency and to be held accountable for results under the Recovery Act. As a means of implementing that goal, guidance has been issued and will continue to be issued to federal agencies, as well as to direct recipients of funding. To date, OMB has issued two broad sets of guidance to the heads of federal departments and agencies for implementing and</p>

managing activities enacted under the Recovery Act.<sup>39</sup> OMB has also issued for public comment detailed proposed standard data elements that federal agencies will require from all (except individuals) recipients of Recovery Act funding.<sup>40</sup> When reporting on the use of funds, recipients must show the total amount of recovery funds received from a federal agency, the amount expended or obligated to the project, project specific information including the name and description of the project, an evaluation of its completion status, the estimated number of jobs created and retained by the project, and information on any subcontracts awarded by the recipient, as specified in the Recovery Act. In addition, the Civilian Acquisition Council and Defense Acquisition Regulations Council have issued an interim rule revising the Federal Acquisition Regulation (FAR) to require a contract clause that implements these reporting requirements for contracts funded with Recovery Act dollars.<sup>41</sup>

State reactions vary widely and often include a mixture of responses to the reporting requirements. Some states will use existing federal program guidance or performance measures to evaluate impact, particularly for on-going programs. Other states are waiting for additional guidance from federal departments or from OMB on how and what to measure to assess impact. While Georgia is waiting on further federal guidance, the state is adapting an existing system (used by the State Auditor to fulfill its Single Audit Act responsibilities) to help the state report on Recovery Act funds. The statewide web-based system will be used to track expenditures, project status, and job creation and retention. The Georgia governor is requiring all state agencies and programs receiving Recovery Act funds to use this system. Some states indicated that they have not yet determined how they will assess impact.

<sup>39</sup>See, OMB memoranda, M-09-10, *Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, February 18, 2009, and M-09-15, *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, April 3, 2009.

<sup>40</sup>OMB, *Information Collection Activities: Proposed Collection; Comment Request*, Federal Register – 74 Fed. Reg. 14824 (Apr. 1, 2009).

<sup>41</sup>74 Fed. Reg. 14639 (March 31, 2009).

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Preserving existing jobs and stimulating job creation and promoting economic recovery are among the Recovery Act's key objectives.<sup>42</sup> Officials in 9 of the 16 states and the District expressed concern about the definitions of jobs retained and jobs created under the Recovery Act, as well as methodologies that can be used for estimation of each. Officials from several of the states we met with expressed a need for clearer definitions of "jobs retained" and "jobs created." Officials from a few states expressed the need for clarification on how to track indirect jobs,<sup>43</sup> while others expressed concern about how to measure the impact of funding that is not designed to create jobs. Mississippi state officials suggested the need for a clearly defined distinction for time-limited, part-time, full-time, and permanent jobs; since each state may have differing definitions of these two categories. Officials from Massachusetts expressed concern that contractors may overestimate the number of jobs retained and created. Some existing programs, such as highway construction, have methodologies for estimating job creation. But other programs, existing and new, do not have job estimation methodologies.

State officials that we spoke with are pursuing a number of different approaches for measuring the effects of Recovery Act funding. For example, Florida's state workforce agency is encouraging recipients of Recovery Act funds throughout the state to list jobs created with the funds in the state's existing online job bank. The Iowa Department of Transportation tracks the number of worker hours by highway project on the basis of contractor reports and will use these reports to estimate jobs created. In New Jersey, state and local agencies will collect or estimate data on the number of jobs created or retained as a result of Recovery Act funds in different ways. For example, the Newark Housing Authority will use payroll data to keep track of the exact number of union tradesmen and housing authority residents employed to turn damaged vacant units into rentable ones. In contrast, New Jersey Transit is using an academic study that examined job creation from transportation investment to estimate the number of jobs that are created by contractors on its Recovery Act-funded

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<sup>42</sup>Recovery Act, § 3(a)(1). Non-federal entities receiving discretionary funds appropriated under the Recovery Act must report on the number of jobs created and retained, among other requirements. Mandatory and entitlement programs are excluded from this requirement. Recovery Act, div. A, title XV, § 1512.

<sup>43</sup>Indirect jobs are jobs created as a result of demand for goods and services generated by direct funding from the Recovery Act.

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construction projects.<sup>44</sup> Beyond employment issues, some Michigan state universities and the state's economic development department are expected to participate in analyses of the potential impact of Recovery Act funds.

Some of the questions that states and localities have about Recovery Act implementation may have been answered in part via the guidance provided by OMB for the data elements and in the Federal Acquisition Regulation, as well as by guidance issued by federal departments. For example, OMB provided definitions for employment, as well as for jobs retained and jobs created via Recovery Act funding. However, OMB did not specify methodologies for estimating jobs retained and jobs created, which has been a concern for some states. Data elements were presented in the form of templates with section by section data requirements and instructions. OMB provided a comment period during which it is likely to receive many questions and requests for clarifications from states, localities, and other direct recipients of Recovery Act funding. OMB plans to update this guidance again within 30 to 60 days of its April 3, 2009 issuance. Some federal agencies have also provided guidance to the states. The U.S. Departments of Education, Housing and Urban Development, Justice, Labor, Transportation, the Corporation for National and Community Service, the National Institutes of Health, and the Centers for Medicare & Medicaid Services have provided guidance for program implementation, particularly for established programs. Although guidance is expected, some new programs, such as the Broadband Deployment Grants, are awaiting issuance of implementation instructions.

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<sup>44</sup>The study estimated that for every \$1 million of transportation infrastructure investment, 11 jobs are created, 70 percent of them are directly related to the investment and 30 percent are indirectly related. (Rutgers University Edward J. Bloustein School of Planning and Public Policy, "Economic Impacts of Planned Transportation Investments in New Jersey" Camden, New Jersey, April 2008.)

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### Concluding Observations and Recommendations: Moving Forward to Clarify Recovery Act Roles and Responsibilities

It has been a little over two months since enactment of the Recovery Act and OMB has moved out quickly. In this period, OMB has issued two sets of guidance, first on February 18 and next on April 3, with another round to be issued within 60 days. OMB has sought formal public comment on its April 3 guidance update and before this, according to OMB, reached out informally to Congress, federal, state, and local government officials, and grant and contract recipients to get a broad perspective on what is needed to meet the high expectations set by Congress and the Administration. In addition, OMB is standing up two new reporting vehicles, Recovery.gov, which will be turned over to the Recovery Accountability and Transparency Board and is expected to provide unprecedented public disclosure on the use of Recovery Act funds, and a second system to capture centrally information on the number of jobs created or retained. As OMB's initiatives move forward and it continues to guide the implementation of the Recovery Act, OMB has opportunities to build upon its efforts to date by addressing several important issues.

These issues can be characterized broadly in three categories: (1) Accountability and Transparency Requirements, (2) Administrative Support and Oversight, and (3) Communications.

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### Accountability and Transparency Requirements

Recipients of Recovery Act funding face a number of implementation challenges in this area. The Act includes many programs that are new or new to the recipient and, even for existing programs, the sudden increase in funds is out of normal cycles and processes. Add to this the expectation that many programs and projects will be delivered faster so as to inject funds into the economy and it becomes apparent that timely and efficient evaluations are needed. The following are our recommendations to help strengthen ongoing efforts to ensure accountability and transparency.

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### Single Audit

The single audit process is a major accountability vehicle but should be adjusted to provide appropriate focus and the necessary level of accountability over Recovery Act funds in a timelier manner than the current schedule. OMB has been reaching out to stakeholders to obtain input and is considering a number of options related to the single audit process and related issues.

**We Would Recommend:** To provide additional leverage as an oversight tool for Recovery Act programs, the Director of OMB should adjust the current audit process to:



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- focus the risk assessment auditors use to select programs to test for compliance with 2009 federal program requirements on Recovery Act funding;
  - provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010; and
  - evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.
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#### Reporting on Impact

Responsibility for reporting on jobs created and retained falls to non-federal recipients of Recovery Act funds. As such, states and localities have a critical role in determining the degree to which Recovery Act goals are achieved. Senior Administration officials and OMB have been soliciting views and developing options for recipient reporting. In its April 3 guidance, OMB took an important step by issuing definitions, standard award terms and conditions, and clarified tracking and documenting Recovery Act expenditures. Furthermore, OMB and the Recovery Accountability and Transparency Board are developing the data architecture for the new federal reporting system that will be used to collect recipient reporting information. According to OMB, state chief information officers commented on an early draft and OMB expects to provide an update for further state review.

**We Would Recommend:** Given questions raised by many state and local officials about how best to determine both direct and indirect jobs created and retained under the Recovery Act, the Director of OMB should continue OMB's efforts to identify appropriate methodologies that can be used to:

- assess jobs created and retained from projects funded by the Recovery Act;
- determine the impact of Recovery Act spending when job creation is indirect;
- identify those types of programs, projects, or activities that in the past have demonstrated substantial job creation or are considered likely to do so in the future. Consider whether the approaches taken to estimate jobs created and jobs retained in these cases can be replicated or adapted to other programs.

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There are a number of ways that the needed methodologies could be developed. One option would be to establish a working group of federal, state and local officials and subject matter experts.

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#### State and Federal Data Collection

Given that governors have certified to the use of funds in their states, state officials are uncertain about their reporting responsibilities when Recovery Act funding goes directly to localities. Additionally, they have concerns about the capacity of reporting systems within their states, specifically, whether these systems will be capable of aggregating data from multiple sources for posting on Recovery.gov. Some state officials are concerned that too many federal requirements will slow distribution and use of funds and others have expressed reservations about the capacity of smaller jurisdictions and non-profits to report data. Even those who are confident about their own systems are uncertain about the cost and speed of making any required modifications for Recovery.gov reporting or further data collection.

Problems also have been identified with federal systems that support the Recovery Act as well. For example, questions have been raised about the reliability of [www.USAspending.gov](http://www.USAspending.gov) (USAspending.gov) and the ability of Grants.gov to handle the increased volume of grant applications. OMB is taking concerted actions to address these concerns. It plans to reissue USAspending guidance shortly to include changes in operations that are expected to improve data quality. In a memorandum dated March 9, OMB said that it is working closely with federal agencies to identify system risks that could disrupt effective Recovery Act implementation and acknowledged that Grants.gov is one such system. A subsequent memorandum on April 8, offered a short-term solution to the significant increase in Grants.gov usage while longer-term alternative approaches are being explored. GAO has work underway to review differences in agency policies and methods for submitting grant applications using Grants.gov and will issue a report shortly.

OMB addressed earlier questions about reporting coverage in its April 3 guidance. According to OMB there are limited circumstances in which prime and sub recipient reporting will not be sufficient to capture information at the project level. OMB stated that it will expand its current model in future guidance. OMB guidance described recipient reporting requirements under the Recovery Act's section 1512 as the minimum which must be collected, leaving it to federal agencies to determine whether additional information would be required for program oversight.

	<p><b>We Would Recommend:</b> In consultation with the Recovery Accountability and Transparency Board and States, the Director of OMB should evaluate current information and data collection requirements to determine whether sufficient, reliable and timely information is being collected before adding further data collection requirements. As part of this evaluation, OMB should consider the cost and burden of additional reporting on states and localities against expected benefits.</p>
Administrative Support and Oversight	<p>At a time when states are experiencing cutbacks, state officials expect the Recovery Act to incur new regulations, increase accounting and management workloads, change agency operating procedures, require modifications to information systems, and strain staff capacity, particularly for contract management. Although federal program guidelines can include a percentage of grants funding available for administrative or overhead costs, the percentage varies by program. In considering other sources, states have asked whether the portion of the State Fiscal Stabilization Fund that is available for government services could be used for this purpose. Others have suggested a global approach to increase the percentage for all Recovery Act grants funding that can be applied to administrative costs. As noted earlier, state auditors also are concerned with meeting increased audit requirements for Recovery Act funding with a reduced number of staff and without a commensurate reduction in other audit responsibilities or increase in funding. OMB and senior administration officials are aware of the states' concerns and have a number of options under consideration.</p> <p><b>We Would Recommend:</b> The Director of OMB should timely clarify what Recovery Act funds can be used to support state efforts to ensure accountability and oversight, especially in light of enhanced oversight and coordination requirements.</p>
Communications	<p>State officials expressed concerns regarding communication on the release of Recovery Act funds and their inability to determine when to expect federal agency program guidance. Once funds are released, there is no consistent procedure for ensuring that the appropriate officials in states and localities are notified. According to OMB, agencies must immediately post guidance to the Recovery Act web site and inform to the "maximum extent practical, a broad array of external stakeholders." In addition, since nearly half of the estimated spending programs in the Recovery Act will be administered by non-federal entities, state officials have suggested opportunities to improve communication in several areas. For example, they wish to be notified when funds are made available to prime recipients that are not state agencies.</p>

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Some of the uncertainty can be attributed to evolving reports and timing of these reports at the federal level as well as the recognition that different terms used by federal assistance programs add to the confusion. A reconsideration of how best to publicly report on federal agency plans and actions led to OMB's decision to continue the existing requirement to report on the federal status of funds in the Weekly Financial and Activity Reports and eliminate a planned Monthly Financial Report. The Formula and Block Grant Allocation Report has been replaced and renamed the Funding Notification Report. This expanded report includes all types of awards, not just formula and block grants, and is expected to better capture the point in the federal process when funds are made available.

**We Would Recommend:** To foster timely and efficient communications, the Director of OMB should develop an approach that provides dependable notification to (1) prime recipients in states and localities when funds are made available for their use, (2) states, where the state is not the primary recipient of funds, but has a state-wide interest in this information, and (3) all non-federal recipients, on planned releases of federal agency guidance and, if known, whether additional guidance or modifications are expected.

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## Agency Comments and Our Evaluation

We provided the Director of the Office of Management and Budget with a draft of this report for comment on April 20, 2009. OMB staff responded the next day, noting that in its initial review, OMB concurred with the overall objectives of our recommendations. OMB staff also provided some clarifying information, adding that OMB will complete a more thorough review in a few days. We have incorporated OMB's clarifying information as appropriate. In addition, OMB said it plans to work with us to define the best path forward on our recommendations and to further the accountability and transparency of the Recovery Act. The Governors of each of the 16 states and the Mayor of the District were provided drafts for comment on each of their respective appendixes in this report. Those comments are included in the appendixes.

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We are sending copies of this report to the Office of Management and Budget and relevant sections to the selected states and the District.

The report will also be available at no charge on the GAO Web site at <http://www.gao.gov>.

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If you or your staffs have any questions about this report, please contact me at (202) 512-5500. Contact points for our offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made major contributions to this report are listed in appendix III-XX.

Sincerely,

A handwritten signature in black ink, reading "Gene L. Dodaro". The signature is fluid and cursive, with a large, stylized "D" and a long horizontal stroke at the end.

Gene L. Dodaro  
Acting Comptroller General of the United States

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*List of Congressional Committees*

The Honorable Daniel K. Inouye  
Chairman  
The Honorable Thad Cochran  
Ranking Member  
Committee on Appropriations  
United States Senate

The Honorable Joseph I. Lieberman  
Chairman  
The Honorable Susan M. Collins  
Ranking Member  
Committee on Homeland Security and Governmental Affairs  
United States Senate

The Honorable David R. Obey  
Chairman  
The Honorable Jerry Lewis  
Ranking Member  
Committee on Appropriations  
House of Representatives

The Honorable Edolphus Towns  
Chairman  
The Honorable Darrell Issa  
Ranking Member  
Committee on Oversight and Government Reform  
House of Representatives

## Appendix I: Objectives, Scope, and Methodology

The Recovery Act specifies several roles for GAO, including conducting bimonthly reviews of selected states' and localities' use of funds made available under the act. As a result, our objectives for this report were to describe (1) selected states' and localities' uses of and planning for Recovery Act funds, (2) approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of the Recovery Act funds they have received to date.

### Selection of States

To address our objectives, we selected a core group of 16 states and the District that we will follow over the next few years to provide an ongoing longitudinal analysis of the use of funds provided in conjunction with the Recovery Act. The selected states are Arizona, California, Colorado, Florida, Georgia, Iowa, Illinois, Massachusetts, Michigan, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas. We selected these states and the District on the basis of outlay projections, percentage of the U.S. population represented, unemployment rates and changes, and a mix of states' poverty levels, geographic coverage, and representation of both urban and rural areas. These states and D.C. contain about 65 percent of the U.S. population and are estimated to receive about two-thirds of the intergovernmental grant funds available through the Recovery Act. Furthermore, they strike a balance between covering a significant portion of Recovery Act funding and obtaining a mix that reflects the breadth of circumstances facing states and localities throughout the country.

### Selection of Programs

To focus our analysis, we examined a set of programs receiving Recovery Act funding that are administered by states and localities. To do this, we reviewed analysis and estimates of Recovery Act funds flowing to states and localities that were done by state and local associations including the National Governors Association, the National Conference of State Legislatures, and the Federal Funds Information for States (FFIS). We also analyzed data from congressional appropriations committees and the Congressional Budget Office (CBO) on the distribution, allocation, and spend out rates of Recovery Act funding.

The programs we selected were streams of Recovery Act funding flowing to states and localities through increased Medicaid Federal Medical Assistance Percentage (FMAP) grant awards, funding for highway infrastructure investment, and the State Fiscal Stabilization Fund (SFSF). Together, they are expected to account for about 91 percent of fiscal year

2009 Recovery Act spending by states and localities. For the FMAP grant awards, we conducted a web-based inquiry, asking the 16 states and D.C. to provide data and information on enrollment, expenditures, and changes to their Medicaid programs and to report their plans to use state funds made available as a result of the increased FMAP. We reviewed states' responses for internal consistency and conducted follow-up with the states as needed. We also spoke with individuals from the U.S. Department of Health and Human Services regarding the changes to the FMAP and the disbursement of increased FMAP funds. In addition, we spoke with individuals from the Centers for Medicare & Medicaid regarding their oversight and guidance to states. For highways infrastructure investment, we reviewed status reports and guidance to the states and discussed these with the U.S. Department of Transportation (DOT) and Federal Highways Administration (FHWA) officials. To understand how the U.S. Department of Education is implementing the SFSF, we reviewed relevant laws, guidance, and communications to the states and interviewed Education officials. Our review of related documents and interviews with federal agency officials focused on determining and clarifying how states, school districts, and public institutions of higher education would be expected to implement various provisions of the SFSF.

We considered programs with large amounts of funding, programs receiving significant increases in funding, new programs, and those with known risks. For example, the Medicaid program is on the GAO high risk list. In addition, we consulted with our internal program experts and outside experts including federal agency inspectors general, state and local auditors, and state and local government associations.

#### Approach in States and Localities on Uses and Plans for Recovery Act Funds

Our teams visited the 16 selected states, localities within those states, and D.C. during March and April 2009 to collect documentation on the plans, uses, and tracking of Recovery Act funds and to conduct interviews with state and local officials. The teams met with a variety of state and local officials from executive-level offices including Governors and their key staff, Comptrollers' Offices, Treasurers' Offices, State Auditors' Offices, Recovery Czars, Inspectors General, senior finance and budget officials, and local officials such as from housing authorities, school districts, police departments, and other key audit community stakeholders to determine how they planned to conduct oversight of Recovery Act funds. The teams also met with state and local agencies administering programs receiving Recovery Act funds, including state Departments of Education, Transportation, and Health and Human Services, and with selected legislative offices in the states. In support of these interviews, we



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Appendix I: Objectives, Scope, and Methodology

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Assessing Safeguards and Internal Controls

developed a series of program review and semi-structured interview guides that addressed state plans for management, tracking, and reporting of Recovery Act funds and activities. These guides focused on identification of risk, risk mitigation, contracting, the internal control environment and safeguards against fraud, waste, and abuse. While in the 16 states and D.C., the teams also met with and interviewed a number of local government officials, whose offices are identified in Appendix 2.

To determine how states and localities plan to track the receipt of, planning for, and use of Recovery Act funds, the state and D.C. teams asked cognizant officials to describe the accounting systems and conventions that would be used to execute transactions and to monitor and report on expenditures. In addition, to assist in the planning of the audit work and for inclusion in their risk assessment framework, we provided the state and D.C. teams with fiscal year 2007 single audit summary information, which was the most recent single audit information available. Single audit information was obtained from the Federal Audit Clearinghouse (FAC) single audit data collection forms and the single audit reports. The single audit summary information provided included : (1) total federal awards expended; (2) whether there were questioned costs; (3) the financial statement audit opinion, number of material weaknesses, and a brief description of each material weakness; and (4) major federal program audit opinion, number of material weaknesses, and a brief description of each material weakness. We examined the Single Audit reports to identify these issues and used that information when interviewing state officials in order to ascertain how they have addressed or plan to address the weaknesses. We also asked auditors to address how they planned to monitor and oversee the Recovery Act funds and whether or not they felt their offices had sufficient capacity to handle any new or increased responsibilities related to the Recovery Act.

Recovery Act Reporting Requirements

To understand the reporting requirements of the Recovery Act, we reviewed the guidance issued by OMB on February 18 and April 3, 2009 and selective federal agency guidance related to grants and to states and localities. We also reviewed an interim rule amending the Federal Acquisition Regulation containing interim reporting requirements for the Recovery Act, issued March 31, 2009.<sup>1</sup> Additionally we studied the OMB issued Information Collection Requirements: Proposed Collection (April 1,

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<sup>1</sup>74 Fed. Reg. 14,639.

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2009) that contains the data elements for the quarterly recipient reports specified in Section 1512 of the Recovery Act. Each of the states and D.C. provided information on its plans to provide assessment data required by Section 1512.

We conducted this performance audit from February 17, 2009, through April 20, 2009, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. Data on states' and localities' plans, uses, and tracking of Recovery Act funds was provided during interviews and follow-up meetings with state and local officials. Given that much of the Recovery Act funding had not yet reached the states and localities, we could not validate nor test the accuracy of the statements made by these officials regarding their accounting and tracking systems. Overall, we determined that the data were sufficiently reliable for the purposes of providing the background information on Recovery Act funding for this report. Our sample of selected states is not a random selection and therefore cannot be generalized to the total population of state and local governments.

## Appendix II: Localities Visited by GAO in Selected States

**Table 5: States and Localities Visited by GAO**

States and the District of Columbia	Localities (or Associations Representing Localities)
Arizona	Regional Public Transportation Authority, Maricopa Association of Governments, City of Phoenix Public Transit Department, City of Phoenix Housing Department, City of Glendale Housing Department, Tempe School District, Peoria Accelerated High School, Maricopa Workforce Connections, City of Phoenix Workforce Connection Division
California	Sacramento Housing and Redevelopment Agency
Colorado	Denver Mayor's Office, Denver City Auditor, Denver Housing Authority, Denver Office of Economic Development
District of Columbia	District of Columbia Housing Authority, Washington Metropolitan Area Transportation Authority
Florida	Florida Association of Counties, Workforce Plus (a regional workforce board for Leon, Gadsden, and Wakulla Counties), Tallahassee Housing Authority, Florida Association of School District Superintendents
Georgia	Atlanta Housing Authority, Atlanta Regional Workforce Board
Iowa	City of Des Moines
Illinois	Chicago Transit Authority
Massachusetts	City of Boston, Massachusetts Bay Transportation Authority
Michigan	City of Detroit Mayor's Office, City of Lansing Mayor's Office, City of Detroit Office of Auditor General, Detroit Public Schools, Lansing School District
Mississippi	Central Mississippi Planning and Development District, The Housing Authority of the City of Jackson
New Jersey	Newark Mayor's Office, New Jersey Transit in Newark, Newark Housing Authority, Newark Public Schools, Trenton Mayor's Office, Trenton Police Department, Trenton Housing Authority, Trenton Board of Education
New York	New York City's Mayor's Office, New York City Budget Director, New York City Comptroller
North Carolina	City of Raleigh, Wake County, North Carolina Association of County Commissioners, North Carolina League of Municipalities
Ohio	Columbus Metropolitan Housing Authority, Franklin County Government, City of Columbus, Columbus City Schools, Local WIA
Pennsylvania	Harrisburg Housing Authority, South Central Workforce Investment Board
Texas	City of Austin Office of the City Auditor, City of Austin-Financial & Administrative Services Department, The Housing Authority of the City of Austin

Source: GAO.

## Appendix III: Arizona

### Overview

**Use of funds:** An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) have made about \$534.6 million in Medicaid FMAP grant awards to Arizona.
  - As of April 1, 2009, the state has drawn down about \$286.3 million, or almost 54 percent of its initial increased FMAP grant awards.
  - Officials plan to use a significant portion of funds made available as a result of the increased FMAP to offset statewide general fund shortfalls.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Arizona was apportioned about \$522 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated \$148.1 million for 26 Arizona projects.
  - As of April 20, 2009, the Arizona Department of Transportation (ADOT) had selected 41 highway transportation projects worth almost \$350 million and had advertised competitive bids on 27 of these projects totaling about \$190 million. The earliest bids will close on April 24, 2009, with projects expected to begin work later this spring.
  - These projects include activities such as preserving pavement, widening lanes and adding shoulders, and repairing bridges and interchanges.
  - Arizona will request reimbursement from the Federal Highway Administration as the state makes payments to contractors.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Arizona was allocated about \$681.4 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. The state plans to submit its application by April 24, 2009, once officials review the latest estimates for the state's fiscal year 2010 budget situation.
  - The state expects funds to be used to improve student assessments, obtain more teachers, and meet federal standards, among other things, in compliance with federal requirements.

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Appendix III: Arizona

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Arizona is also receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act (ESEA), (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA); several housing programs such as the Low-Income Housing Tax Credit (LIHTC) Assistance program; and programs under the Workforce Investment Act to help provide employment-related services, among other things. Plans to use these funds are discussed throughout this appendix.

**Safeguarding and transparency:** The state government created a new Office of Economic Recovery within the Office of the Governor, the purpose of which is to coordinate the use of Recovery Act funds across state agencies and to ensure accountability for and transparency in the use of these funds. In addition, to meet Recovery Act requirements, the state comptroller noted that Arizona intends to add new codes to its central accounting system to track Recovery Act funds separately and work with state agencies that have their own accounting systems to ensure that they can also track funds separately. The state has issued guidance on managing the funds, and has plans to publicly report its Recovery Act spending, although officials have said that the state may not be aware of all funds sent directly by federal agencies to other entities, such as municipalities and independent authorities. The officials also identified other challenges, such as ensuring that recipients can report on their use of funds and that, where applicable, funds are used to supplement and not supplant state funds that support relevant affected programs. State and local officials noted that they expect to use existing internal controls and monitoring techniques to safeguard Recovery Act funds, but are concerned about having enough resources to do so. State departments were in the early stages of addressing some of these challenges, and are awaiting further guidance from the federal government on these issues.

**Assessing the effects of spending:** Arizona state agencies and select localities that we met with expect to use or enhance existing performance metrics to assess the results achieved through Recovery Act funding, unless the federal government requires new metrics that will need to be developed. State officials were unclear, however, on how to determine the number of jobs created and saved by certain Recovery Act funds and were awaiting further guidance from the federal government.

## Arizona Beginning to Use Recovery Act Funds

Arizona has begun to use some of its Recovery Act funds as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, Arizona has drawn down \$286.3 million in increased FMAP grant awards, which is almost 54 percent of its total awards of \$534.5 million. Officials plan to use a significant portion of funds made available as a result of the increased FMAP to offset shortfalls created by reductions implemented to balance the budget. The state used the initial funds made available as a result of the increased FMAP to meet payroll and to avoid serious cash-flow problems.

<sup>1</sup> See Recovery Act § 5001.

<sup>2</sup> Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and to undertake other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Arizona has provided this certification.

As of April 20, 2009, the Arizona Department of Transportation (ADOT) had selected 41 highway transportation projects to be funded with Recovery Act dollars.<sup>3</sup> These projects are worth approximately \$350 million of the state's total \$521.9 million apportionment. These include projects such as pavement preservation, widening lanes and adding shoulders, and bridge and interchange repair. As of April 20, 2009, the state had advertised 27 projects worth about \$190 million with the earliest bids to close on April 24, 2009, and projects expected to begin work this spring. Among the projects that have been advertised for bid are the widening of Interstate 10 in Maricopa County, repaving of state routes, making safety improvements to a state route, and improving intersections. Among the first advertisements to close will be the widening of a shoulder within the Tonto National Forest, on State Route 87. The cost of this project is estimated at approximately \$6.8 million, and is estimated to take 150 days to complete. Bids will close on April 24, 2009.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures it will take action

<sup>3</sup>As of April 16, 2009, the U.S. Department of Transportation had obligated \$148.1 million for 26 Arizona projects. For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Arizona's initial SFSF allocation is \$681.4 million. The state plans to submit its application for funds by May 4, 2009, but according to state education officials, they are waiting for the legislature to propose a 2010 budget for their programs before they can definitely decide how they will spend the funds. Generally, the state expects that recipients, such as local school boards, will use their allocations to improve the tools they use to assess student performance and determine to what extent performance meets federal academic standards, rehire teachers that were let go because of prior budget cuts, retain teachers, and meet the federal requirement that all schools have equal access to highly qualified teachers, among other things. Funds for the state universities will help them maintain services and staff as well as avoid tuition increases.

### Recovery Act Funds Supporting Other Programs

In addition to stabilization funding to support education through the state fiscal stabilization fund, a senior official from the Arizona Department of Education noted that, as of April 3, 2009, Arizona had received \$97.5 million for programs under Title I, Part A of ESEA. The funds will be used to improve assessments to meet federal standards, enrich teacher qualifications, avoid more teacher layoffs, improve poorer performing schools, and ultimately improve student performance, among other things. The state had also received about \$89.2 million for programs under IDEA, Part B, which provides funds for public education to children with disabilities. According to state Department of Education officials, these funds will be used to hire more teachers to serve students with special needs, among other things. se programs, The state education officials said that they had prepared estimated allocations for the No Child Left Behind Recovery Act funds to the local school districts, which in turn will prepare and submit applications before they can use the funds.

Arizona is also eligible to receive Recovery Act funds for several housing programs including the Low-Income Housing Tax Credit (LIHTC) Assistance program. The Arizona Department of Housing received notice that it will receive approximately \$32 million to provide gap financing for LIHTC projects which provide funding for development of low income housing. Finally, the state Department of Economic Security had received approximately \$43 million in Recovery Act funding anticipated for Workforce Investment Act programs to be used for adult, youth (including a summer youth program), and dislocated worker services.



**State Agencies and Select Localities Will Use Recovery Act Funds to Restore Programs That Suffered Past Budget Cuts and Will Track These Funds Separately, but Expect Some Challenges**

Faced with deteriorating revenue projections, declining consumer confidence, a depressed real estate market, and a requirement to balance its budget, Arizona officials believe that much of the money the state will receive in Recovery Act funds will relieve some of the state's immediate fiscal pressures. State officials envision that funds made available as a result of the Recovery Act will be used to support program budgets that had been reduced in the state's efforts to balance the budget. Arizona has about \$7 billion in its General Fund with a current budget of about \$10 billion. State officials are working to close a budget gap of about \$1.3 billion for fiscal year 2008, an estimated budget gap of about \$2.1 billion for state fiscal year 2009 and about \$2.8 billion for fiscal year 2010 through reductions and other strategies. These strategies were limited to some extent, because voter propositions protect major programs from significant cuts, including Medicaid, education, and corrections, meaning other programs must absorb the cuts. The state's budget imbalance has been complicated by lower-than-anticipated revenues. For example, state fiscal year 2009 revenue is significantly lower than estimated and has left the state unable to support previously approved spending levels. Arizona's Budget Office has estimated its future revenues and expenditures for each fiscal year through 2014. It projects an increasing deficit in each fiscal year, from \$2.1 billion in 2009 to \$4.1 billion in 2014, a situation which most likely would mean continued cuts. The state's Budget Stabilization Fund, known as its "rainy day" fund—a reserve fund built up during more favorable economic conditions to be used during difficult economic times—has been depleted.

As of April 13, 2009, decisions about finalizing the fiscal year 2010 budget were still in flux in part because Governor Brewer—only in office since January after the former Governor, Janet Napolitano, became Secretary of the U.S. Department of Homeland Security—has not issued a formal budget proposal. The Governor recognized that further reductions in government services may be necessary to help close the significant deficit between state revenues and expenditures. Given this, in early March, the Governor certified that the state would accept the funds made available by the Recovery Act and use certain funds to create jobs and promote economic growth within the state. Because of the state's economic and budgetary challenges, some state agency and local officials we met with expected to use the funds as they had been using them under their existing programs and did not expect to use Recovery Act funding on new initiatives. They also were confident recipients had sufficient critical uses for the funds and could use them immediately.

However, state officials expressed concerns that using Recovery Act funds to make longer term operational and program commitments would mean higher future state spending that would not be sustainable once Recovery Act funds were no longer available, given the state of the economy. As a result, officials from one state agency explained that they are advising subrecipients to spend their funds on shorter term projects. Furthermore, with program budgets being cut to help relieve fiscal pressures, some state officials have said it may be challenging to ensure compliance with provisions requiring certain Recovery Act funds to be used to supplement and not supplant FY 2010 program funds. Officials with the state Department of Education, however, had one concern about passing the supplanting test. They said that it was unclear whether states could treat Recovery Act funds provided under the fiscal stabilization program as "state" funds versus "federal" funds. If they could use the funds as state resources, they would be able to meet the supplanting restrictions, but if not, they would have serious challenges in complying, jeopardizing the use of the funds. On the other hand, some state officials and program managers did not think it would be difficult to demonstrate they were not supplanting state funds in part because state funding for the programs had already been cut so significantly—in other words, there were few state funds to supplant. For example, they did not think it would be difficult to show that activities supported with Recovery Act resources, such as keeping teachers, could only be accomplished with federal support.

One issue raised by officials in the Office of the Governor and within some state and local program offices was covering the costs to oversee and track the use of the Recovery Act funds, given past budget cuts, staff reductions, and increasing workloads—for example, increasing numbers of unemployed individuals who want services. These officials noted that their service delivery capacity will be challenged to administer funds flowing into eligible programs. Some of the officials wondered what flexibility they had to use some of the Recovery Act funds to cover administrative costs. On the other hand, some state agency officials said that they expected to be able to oversee and track Recovery Act funds with existing resources because funding to current programs that had administrative processes in place would be increased. In still other cases, Recovery Act funds will be disbursed through existing grant programs that may provide for a certain percentage of funds to be used for administration.

**The State Has a System to Track How It Is Using Recovery Act Funds but Cannot Ensure Localities Will Be Able to Meet the Act's Reporting Requirements**

The state comptroller told us that the state's existing accounting system will have new accounting codes added in order to segregate and track the Recovery Act funds separately from other funds that will flow through the state government. Because some larger agencies and program offices maintain their own accounting systems, the Arizona General Accounting Office has issued guidance to state agencies on their responsibilities, including how they are to receive, disburse, tag, or code funds in their accounting systems; track funds separately; and, to some extent, report on these federal resources. State officials we spoke with noted that they do not foresee that it will be difficult to track Recovery Act funds separately from other funds. However, an official in the state Department of Economic Security noted that the Recovery Act funds will stress the tracking and reporting capacity of the financial management systems they use because the systems are old, are not very flexible, and were not designed for these purposes. The official said that the systems must be enhanced to provide the capacity needed for Recovery Act funds and that they are working to design a solution for this problem.

Department heads and program officials generally expect that they will require subrecipients, through agreements, grant applications, and revised contract provisions, to track and report Recovery Act funding separately. For example, unemployment program managers said they were issuing new intergovernmental agreements with localities to cover new reporting requirements. However, several of the state officials raised questions about the tracking and reporting abilities of some local organizations, such as small, rural entities, boards or commissions, or private entities not used to doing business with the federal government. Furthermore, several of the state department officials acknowledged that either some state agency information systems have data reliability problems that will have to be resolved, or they had subrecipients that in the past had problems providing timely and accurate reporting, but said that they would work with these entities to comply, and also had sanctions to use as a last resort. Furthermore, state officials expressed some concern that the new requirement to provide financial reports on subrecipients' use of funds within 10 days after a quarter ends may be challenging to meet by both state and local entities, because they may not have actual data in time to meet this reporting time frame.

Finally, the state may lack the ability to track the portion of Recovery Act funds going directly to recipients other than Arizona government agencies, such as independent state authorities, local governments, or other entities. State officials expressed concern that they may not be able to track and

report Recovery Act funds when these entities receive the monies directly from federal agencies rather than through state agencies.

**State Agencies and Localities Are Expecting to Use Existing Internal Controls to Safeguard Recovery Act Funds, Although in Some Cases, Resource Constraints Could Affect Oversight**

Overall, the state agency and local officials that we spoke with expect that their existing internal controls and techniques to manage any potential risks posed to Recovery Act funding will be sufficient and effective to safeguard Recovery Act funds, unless additional requirements are mandated by the federal government that generate the need to change business processes. These controls and techniques include submitting financial and performance reports for review, as well as conducting supervisory and compliance reviews, on-site inspections, external audits, and audits by the state Auditor General. Although Arizona is largely decentralized—state agencies and localities have responsibility for monitoring and are accountable for their respective Recovery Act funds—the state executives are reaching out to the state agencies to help ensure they are ready. For example, the state budget director met with the heads of the programs potentially receiving Recovery Act funds to gauge each program's preparedness. In addition, a number of state agencies were conducting or had plans to conduct meetings, training, and outreach to funding recipients to help them understand the goals and objectives of the act and their responsibilities for managing the funding it would provide. Similarly, in early April 2009, the state's General Accounting Office released a technical bulletin, the purpose of which was to establish consistent policies and procedures that all state agencies receiving Recovery Act funds must "immediately implement in order to effectively manage activities under the act." A senior official in the state comptroller's office said that office plans to conduct a survey to inventory current internal controls at state agencies to help ensure controls are in place to limit the risk of fraud, waste, abuse, and mismanagement of Recovery Act funds.

Several risks still to be addressed have been identified as a result of using audits as an internal control. For example, Arizona's fiscal year 2007 Single Audit report<sup>4</sup> identified a number of material weaknesses related to the state Department of Education. The report identified a material weakness involving IDEA in which the state department had not reviewed subrecipients to ensure that federal awards were used for authorized purposes in compliance with laws, regulations, and the provisions of

<sup>4</sup>Arizona's fiscal year 2007 Single Audit report is the most recent report available.

contracts or grant agreements. The audit report also identified one financial reporting material weakness related to the state Department of Administration's ability to prepare timely financial statements, including its Comprehensive Annual Financial Report (CAFR). This is mostly because many of the larger state agencies maintain separate accounting systems and submit financial data to the Department of Administration for inclusion in its consolidated financial statements. In fiscal year 2007, the CAFR was issued in June 2008, approximately 6 months after the scheduled deadline. According to the Auditor General's Office, the fiscal year 2008 CAFR will also be completed late, as the last agency submitted its financial statement on March 9, 2008. According to the Auditor General's Office, this control deficiency affects the timeliness of financial reporting, which affects the needs of users. It is especially important that Arizona try to address the timeliness issue with regard to financial statements given the number and strict reporting timelines that are imposed on the state under the Recovery Act. For most of the other programs, managers stated that they had no outstanding material weaknesses and that any past weaknesses had been brought into compliance.

According to state officials, another area of risk that the state agency is trying to manage is that some Recovery Act funds, particularly in the transportation area, are reimbursable, meaning that either ADOT or localities will have to spend funds from their own budgets until they are reimbursed by Recovery Act funds. Because of the state's challenging financial situation, it may be a challenge for some state and local government entities to spend the funds up front with the limited cash they have on hand. This is particularly true for rural transit projects. According to an ADOT official, to address this risk, they are vetting applications for rural transit funds closely, with an eye toward granting funds only to those localities that have shown they have the cash on hand to pay up front for the costs of the rural transit projects.

**State Agencies and Localities Will Continue or Enhance Current Monitoring Techniques to Oversee Recovery Act Funds, but in Some Cases, Reduced Resources Could Pose Challenges**

Representatives of a number of state executive offices, state agencies, and select localities reported that they would at a minimum continue to monitor Recovery Act funding as they had monitored federal funding provided to these same programs in the past. They expected to meet the financial monitoring, performance measurement, and accountability requirements using existing systems and reports, unless the federal government institutes any new requirements that would require changes to their systems and processes. The entities were still waiting for further guidance from the federal government to determine any needed changes. In some cases, agencies had plans to increase monitoring. For example, according to officials for the Arizona Division of the Federal Highway Administration (FHWA), they plan on increasing the number of site visits on projects that use Recovery Act funds. Similarly, state transportation officials will require that contractors report the Recovery Act dollars spent and the jobs they created as part of their regular reports to the state.

To some extent, Arizona is providing the public an opportunity to monitor how the state is using Recovery Act funding and what it is achieving with these funds through a Web site, [azrecovery.gov](http://azrecovery.gov), where the state has posted links to program funding levels, guidance, and intended uses of Recovery Act money, and intends to post reports on the use of funds, among other things.

However, several state officials expressed concern that the Recovery Act did not provide funding specifically for state oversight activities, despite their importance in ensuring that the Recovery Act funds are used appropriately and effectively. Officials within state executive offices that are coordinating oversight activities—such as the Office of Economic Recovery and the Comptroller's Office—stated that they will be challenged to oversee compliance with Recovery Act funding requirements within their existing staffing levels, given that the state currently has a hiring freeze to help relieve its budget deficits. For example, the Arizona General Accounting Office within the state Department of Administration has experienced a reduction of staff from 74 to 50, posing challenges to its increased oversight responsibilities. The Department of Economic Security, which manages workforce investment programs and human services programs, among other responsibilities, has an estimated 8,214 staff on furloughs and has laid off about 800 staff members as well. Similarly, a Department of Housing official stated that the office currently has a vacancy rate of about 15 percent because of the hiring freeze. Furthermore, the state Auditor General reported that its staffing levels are nearly 25 percent below the authorized staffing level of 229 full time equivalents.

**State Agencies and Localities Will Use Existing Performance Measures to Gauge the Impacts of Recovery Act Funding and Are Waiting for Federal Guidance on How to Implement New Measures the Act Requires, Especially on Jobs Created and Saved**

State agencies and the select localities that we spoke with expected to use existing performance metrics to assess results achieved through Recovery Act funding, but were also looking for more guidance from the federal government on how to comply with new assessment requirements under the act. Agency officials generally stated that because the Recovery Act funds are for pre-existing programs, they will continue to use their existing performance metrics to assess impacts. For example, the Arizona Criminal Justice Commission, which oversees among other things the Edward Byrne Memorial Justice Assistance Grants, tracks a wide list of both short-term and long-term performance measures that assess the effectiveness of law enforcement projects funded by the grants. Short-term measures include increasing the number of units that report high program quality, while long-term measures include changing crime rate percentages in communities. Commission officials stated that they will continue to track these measures for Recovery Act funding, in addition to any new measures required under the act. Likewise, administrators at a local school district we visited stated that they have a department that uses a system to track the performance for every school and every student in the school district. The officials stated that they will use the same measures to track school and student performance improvements using Recovery Act funds.

However, officials were unclear as to how to determine the number of jobs created and saved by certain Recovery Act funds, new measures required by the act. State education officials noted that the act is vague about determining the number of teachers who would have been laid off in the absence of Recovery Act funding. Although a state housing official expected that her office would have the capabilities to assess results, such as job creation and economic output, local housing officials stated they may have difficulty doing so. State and local officials were waiting for additional guidance from the federal government on how to implement measures for jobs created and saved, as well as any new measures required under the act.

**Arizona's Comments on This Summary**

We provided the Governor of Arizona with a draft of this appendix on April 17, 2009. The Director of the Office of Economic Recovery responded for the Governor on April 20, 2009. In general, the state agreed with our draft and provided some clarifying information which we incorporated. The state also provided technical suggestions that were incorporated, as appropriate.

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**Staff****Acknowledgments**

In addition to the contacts named above, Kirk Kiester, Assistant Director; Joseph Dewechter, analyst-in-charge; Lisa Brownson; Aisha Cabrer; Alberto Leff; Jeff Schmerling; and Margaret Vo made major contributions to this report.



## Appendix IV: California

### Overview

**Use of funds:** An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

#### ✓ Medicaid Federal Medical Assistance Percentage (FMAP) Funds

- As of April 3, 2009, Centers for Medicare & Medicaid Services (CMS) had made about \$3.331 billion in increased Federal Medical Assistance Percentage (FMAP) grant awards to California.
- As of April 1, 2009, the state has drawn down about \$1.5 billion, or 45.4 percent of its initial increased FMAP grant awards.
- Funds made available as a result of increased FMAP will help offset the state's general fund budget deficit, according to California officials.

#### ✓ Transportation—Highway Infrastructure Investment

- California was apportioned about \$2.570 billion for highway infrastructure investment on March 2, 2009 by the U.S. Department of Transportation.
- Under a state law enacted in late March 2009, 62.5 percent of funds (\$1.606 billion) will go to local governments for projects of their selection.
- Of the remaining 37.5 percent (\$964 million), \$625 million will go to State Highway Operation and Protection Program (SHOPP) projects for highway rehabilitation, eligible maintenance and repair; \$29 million will fund Transportation Enhancement projects; and \$310 million will be loaned to fund stalled capacity expansion projects.
- As of April 16, 2009, the U.S. Department of Transportation had obligated \$261.4 million for 20 California projects.
- California will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.

#### ✓ U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)

- California was allocated about \$3.993 billion from the initial release of these funds on April 2, 2009 by the U.S. Department of Education.
- Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and they will implement strategies to meet certain educational requirements, including teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. California's application was approved by the U.S. Department of Education on April 17, 2009 and the state is now eligible to draw funds for local school districts and universities.
- Approximately \$3.266 billion of the \$3.993 billion (81.8 percent) must be spent on education. The remaining \$727 million (18.2 percent) can be spent at the Governor's discretion and is expected to be directed to public safety. Of the funds devoted to education, the majority will be spent on primary and secondary education.

California is receiving additional Recovery Act funds under other programs, such as Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA), (commonly known as No Child Left Behind); the Individuals with Disabilities Education Act, Part B, and workforce training programs under the Workforce Investment Act (WIA).

**Safeguarding and transparency:** The Governor established the California Federal Economic Stimulus Task Force to ensure both accountability and transparency in how funds are spent, consistent with the Recovery Act and the state's own goals. The Task Force will also manage California's recovery Web site ([www.recovery.ca.gov](http://www.recovery.ca.gov)), the state's principal vehicle for reporting on the use and status of Recovery Act funds. In addition, on April 3, 2009, California appointed a Recovery Act Inspector General to make sure Recovery Act funds are used as intended and to identify instances of waste, fraud, and abuse. California intends to use its existing accounting system to track funds flowing through the state government. Although California will publicly report its Recovery Act spending, officials have said that the state may not be aware of all federal funds sent directly to other entities, such as municipalities and independent authorities. The California State Auditor has raised concerns about internal controls at various state agencies that could affect accountability for Recovery Act funds, and will take this into account when assessing risk during her current audit planning efforts.

**Assessing the effects of spending:** According to state officials, California has begun to develop plans to assess the effects of Recovery Act spending. However, they are waiting for further guidance from the federal government, particularly related to measuring job creation.

### California Beginning to Use Recovery Act Funds

California has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible

states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

Under the Recovery Act, California will receive increased FMAP grant awards of at least 61.6 percent, up from 50 percent. As of April 1, 2009, California has drawn down \$1.5 billion, or 45.4 percent of its initial FMAP grant awards. Initially, the state could not obtain increased FMAP funds because the state reduced its eligibility period for children from 12 months of continuous eligibility to 6 months, effective January 1, 2009. However, because this change was suspended on March 27, 2009 and eligibility was restored to any children affected, the state has been able to draw down increased FMAP funds. Officials plan to use funds made available as a result of the increased FMAP to offset the state's general fund budget deficit.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

executive must certify that the state or local government to which the funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. California provided these certifications but noted that the state's level of funding was based on the best information available at the time of the state's certification.<sup>3</sup>

According to state sources, under a state law enacted in late March 2009, 62.5 percent of funds (\$1.606 billion) will go to local governments for projects of their selection. Of the remaining 37.5 percent (\$964 million), \$625 million will go to State Highway Operation and Protection Program (SHOPP) projects for highway rehabilitation, eligible maintenance and repair; \$29 million will fund transportation enhancement projects; and \$310 million will be loaned to fund stalled capacity expansion projects.<sup>4</sup> As of April 16, 2009, the U.S. Department of Transportation had obligated \$261.4 million for 20 California projects.<sup>5</sup> These projects consist of rehabilitating roadways, pavement, and rest areas as well as upgrading median barriers and guardrails. For example, a \$33 million project is being funded to rehabilitate a road in San Jose.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures it will take action to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

<sup>3</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>4</sup>The state is using the \$310 million to jump-start stalled highway projects, which will then be repaid to fund other SHOPP projects once bonds can be issued.

<sup>5</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term "obligation of funds" to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

## Appendix IV: California

California's initial SFSF allocation is \$3.993 billion. Approximately \$3.266 billion of this money (81.8 percent) must be spent on education. The remaining \$727 million (18.2 percent) can be spent on public safety and other government services (including education). California officials told us that the Governor plans to recommend to the State Legislature that the funds be spent on the Department of Corrections.<sup>6</sup> Like other states, California will receive its SFSF funds in two phases. California's application was approved by the U.S. Department of Education on April 17, 2009, and the state is now eligible to draw funds for local school districts and universities. Of the \$3.266 billion for education, the state plans to spend the maximum amount possible under Recovery Act formulas—approximately \$2.57 billion on primary and secondary education and \$537 million on higher education, for the purpose of restoring funding to 2008-2009 levels. The remaining \$164 million will be used to restore education funding in future years. These funds will help ensure that primary and secondary schools and institutions of higher education have the resources they need to avert cuts and retain teachers and professors.

#### Overall Management and Reporting of Recovery Act Funds Are Being Centrally Coordinated

The Governor and his administration are setting the overall policy for coordination of and accountability for Recovery Act funds. Prior to the enactment of the Recovery Act, the Governor's office formed nine working groups organized around broad program areas (e.g., transportation, environment, etc.) and comprising representatives of the Department of Finance, program departments, the legislative branch, and California's Washington, D.C. office. The working groups worked with the California congressional delegation to estimate the effects of the Recovery Act and to lobby for changes helpful to the state. The Recovery Act was enacted on February 17, 2009, and California signed a state certification letter on March 5 stating that the state would request and use certain Recovery Act funds to create jobs and promote economic growth (California was the first state to do so).

Initially, the Department of Finance, the Director of which is appointed by the Governor, was the focal point for working with state agencies to prepare to meet Recovery Act accountability and reporting requirements. In late March 2009, the Governor's office established the California Federal Economic Stimulus Task Force, which is responsible both for

<sup>6</sup>As required by California's constitution, all money drawn from the state's treasury must be appropriated by the State Legislature.

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Appendix IV: California

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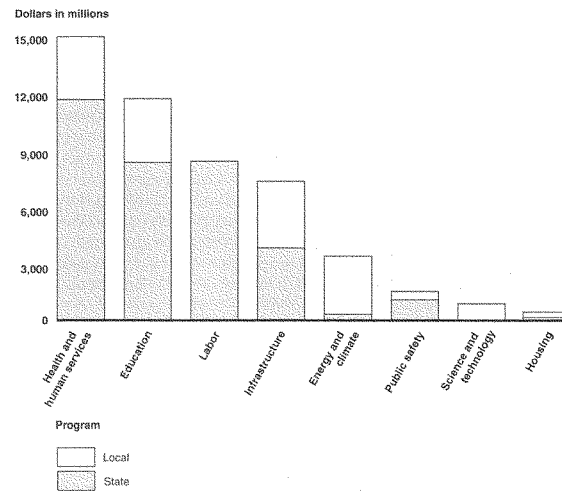
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tracking Recovery Act funds that come into the state and ensuring that those funds are spent efficiently and effectively. The task force is chaired by the Deputy Chief of Staff to the Governor and Director of the Governor's Office of Planning and Research, and will include one representative from the administration for each of the main program areas that will receive funds. The Chief Deputy Director of Finance will serve as deputy coordinator of the task force and will be responsible for, among other things, tracking the funds coming into the state. The Chief Operating Officer of the Department of Finance will oversee the accountability and auditing functions of the task force.

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State Agencies and  
Localities Are Developing  
Spending Plans, but in  
Some Cases Are Awaiting  
Further Guidance and  
Final Determination of  
Amounts to Be Received

In total, as of March 27, 2009, the state of California estimates that the state and its localities will receive approximately \$48.3 billion for various programs, including health, education, and infrastructure. (see figure 4.) Of this, about \$14 billion will go directly to local governments and the other \$34 billion will go to the state.

**Figure 4: California State and Local Recovery Act Funding**

Source: Department of Finance @ [www.recovery.ca.gov](http://www.recovery.ca.gov) (March 27, 2009).

The extent to which spending decisions have been made varies by program in California, with some uses determined while others are still unknown. For example, for some funding, like the \$10 billion made available as a result of the increased FMAP, all or most is formula driven, and the application of funds is already determined. Likewise, for public transit investment grants and fixed-guideway infrastructure programs (due to receive approximately \$1.019 billion in Recovery Act funds, according to Federal Transit Administration officials), all or most of the funding is formula driven, but local priority-setting processes will determine which projects will be funded. For education (receiving about \$11.8 billion in Recovery Act funds), while the majority of allocations to school districts are based on formulas, education officials told us that spending decisions

will largely be made at the local level.<sup>7</sup> Officials from the Sacramento Housing and Redevelopment Agency (SHRA)—one of the state's 55 public housing authorities hoping to receive a portion of Recovery Act funding from the formula-based Public Housing Capital Fund—stated that they have begun to prioritize how funds will be used. Contracts will be awarded by SHRA for bids received within 120 days on projects listed in its 5-year Capital Fund Plan. State officials from the Department of Housing and Community Development are not sure how much funding another program, the Neighborhood Stabilization Program, will receive. Officials told us that their plans for spending the money will be determined by the amount received.

In some instances, state officials have sought federal guidance on the use of certain funds. For example, California Employment Development Department (EDD) officials told us that they hoped to receive additional federal guidance clarifying whether California, through its legislative budget process, can use all discretionary Workforce Investment Act funding through Recovery Act funds to offset employment and training program general fund costs in either the California Department of Corrections and Rehabilitation or the California Conservation Corps. EDD officials noted that using the discretionary funds in this way might contradict recent U.S. Department of Labor guidance, which only allows funds to be used for new programs and not to replace state or local funding for existing programs. State officials are also seeking guidance from CMS regarding policies on payments for in home support services funded by Medicaid. State officials are also uncertain whether Recovery Act funds can help pay for the increased costs of administering, overseeing, and auditing Recovery Act program funds and stated that federal guidance, thus far, has not addressed these questions.

In some cases, state agencies face deadlines for using their funds. Caltrans must obligate at least half of certain Recovery Act funds within 120 days of when the funds were apportioned by the Department of Transportation or the funds will be redistributed to other states.<sup>8</sup> Caltrans did not foresee

<sup>7</sup>State education officials have provided some guidance to local education agencies on appropriate uses for Recovery Act money, and plan to provide more, both formally and informally, as it becomes available from the federal government.

<sup>8</sup>These provisions are applicable only to those funds apportioned to the state and not to those funds required by the Recovery Act to be suballocated to metropolitan, regional and local organizations.



problems meeting this deadline. Caltrans officials further stated that most projects could be completed within 1 year; however, project completion time lines and specific project funding outlays by year have not been finalized. Caltrans officials stated that some project construction may begin by early-May 2009. In another case, the Tax Credit Allocation Committee (TCAC) must commit at least 75 percent of the \$325.9 million in Recovery Act's Tax Credit Assistance Program funds by February 17, 2010. TCAC did not foresee problems meeting this deadline. TCAC officials told us that they have a system in place to quickly identify recipients and that they are planning to make sure to comply with the timeline as reflected in regulations.

**Recovery Act Funds Will  
Help but Not Resolve  
California State Budgetary  
Pressures**

The state's economy and California state revenues have been severely affected by the national recession and financial market credit crunch. In March 2009, California's unemployment rate rose to 11.2 percent, 2.7 percentage points higher than the national average. In February, according to RealtyTrac, California posted the nation's third highest state foreclosure rate, behind Nevada and Arizona, with 1 in every 165 housing units in foreclosure. On March 19, Fitch Investor Services downgraded California General Obligation bonds to an "A" rating, the lowest current rating of any state.

State general fund revenues are projected to fall in state fiscal year 2008-2009 by \$15.1 billion, or 14.7 percent, from fiscal year 2007-2008.<sup>9</sup> In January 2009, the fiscal year 2009-2010 Governor's Budget projected that the state would end the state fiscal year with a \$41.6 billion deficit if no corrective actions were taken. In response, the State Legislature and the Governor agreed to a \$42 billion package of solutions. As described by state sources, this package includes reducing spending, temporarily increasing taxes, using funds made available as a result of the Recovery Act, and borrowing from future lottery profits.<sup>10</sup> The budget package depends, in part, on voter approval of six different propositions at a May

<sup>9</sup>The California state government fiscal year is July 1 to June 30.

<sup>10</sup> As part of the budget agreement, the Treasurer and the Director of the Department of Finance had to determine by April 1, 2009, if by June 30, 2010, the state would use more than \$10 billion in funds made available as a result of the Recovery Act to offset its general fund budget deficit. If so, the state would rescind \$948 million in spending cuts and about \$1.8 billion in tax increases under the budget agreement. On March 27, 2009, the two state officials estimated that only \$8.2 billion would be applied as a general fund budget offset, and therefore the spending cuts and tax increase were retained.

19, 2009, special election. If three of these propositions are approved, the state Legislative Analyst's Office (LAO) estimates the package will reduce the state's budget deficit by \$6 billion.

Unfortunately, the state's economic condition since the release of the Governor's budget in January 2009 has continued to deteriorate. Even if the May 19, 2009, propositions pass, and the state uses \$8.2 billion in funds made available as a result of the Recovery Act, the LAO estimates an \$8 billion deficit in 2009-2010. Consequently, the State Legislature and the Governor may need to work on additional budgetary solutions to rebalance the 2009-2010 budget following the May 2009 budget update. On February 3, 2009, the California State Auditor added the state's budget condition to its list of high-risk issues facing the state.

### Plans for Oversight and Control of Recovery Funds Are Still Evolving

State officials are working to get the necessary guidance and systems up and running that will allow for a comprehensive and accurate accounting of California Recovery Act funds. As previously mentioned, the California Federal Economic Stimulus Task Force is responsible for tracking Recovery Act funds and ensuring that they are spent efficiently and effectively. The state's new recovery Web site ([www.recovery.ca.gov](http://www.recovery.ca.gov)) will serve as the primary tool to fulfill federal reporting and accountability requirements consistently throughout the state. A representative from each state agency is tasked with ensuring that data required by federal Recovery Act reporting requirements are available on the state Web site. Development of the related processes and procedures to accumulate and consolidate the spending data is underway. State officials also plan to use the Web site to provide the public with up-to-date information about federal funds received by the state, how those dollars are being spent, and, through the use of digital mapping, the geographic distribution of expenditures.

### Internal Control and Tracking Is Expected to Be Achievable for State-Level Funds, but Concerns Exist Over Funds Provided to Localities

The state intends to rely heavily on existing systems to track and account for Recovery Act funds. State agency officials generally told us that their existing accounting systems, enhanced with newly created codes for Recovery Act funds, will enable them to separately track and monitor how state and local agencies spend Recovery Act funds that pass through the state. For example, California Department of Education officials told us that the department already has a consistent accounting structure in place for tracking and reporting on how federal funds are used. The department plans to create separate accounting codes within that structure to track and report how the different programmatic funds received through the

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Recovery Act are used. According to the officials, the department will provide those codes to the local education agencies (LEA), as well as instruct them on what the codes mean. However, some officials still expressed concerns about the ability of LEAs to consistently maintain accountability for funds. For example, a Department of Finance official with responsibility for education program budgets stated that there are over 1,000 school districts in California, and they possess varying levels of sophistication in their accounting systems. While the state will be providing guidance to help ensure proper accountability, this official expects some districts may face challenges complying.

Most state program officials told us that they will apply the same controls and oversight processes that they currently apply to other program funds. For example, the California Employment and Development Department has an independent division that conducts monitoring, audits, and evaluations to guard against mismanagement, waste, fraud, and abuse. The effectiveness of internal controls at the local level, however, is unknown for some programs. Caltrans officials, for example, stated that while extensive internal controls exist at the state level, there may be control weaknesses at the local level.<sup>11</sup> Caltrans is collaborating with local entities to identify and address these weaknesses. Additionally, Caltrans has conducted workshops and other outreach activities to ensure that regions and localities are fully informed regarding requirements for the tracking and expenditure of Recovery Act funds, and would like to increase its capacity to provide oversight, particularly at the local level.

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**Various Audit Functions  
Will Provide Oversight**

California intends to use existing internal and independent audit functions and a new inspector general to oversee Recovery Act funds received by the state. The Office of State Audits and Evaluations (OSAE) is an internal audit function within the Department of Finance which performs audits of various state funds and programs, including those receiving Recovery Act funds. According to state officials, OSAE is also responsible for ensuring compliance with the state's Financial Integrity and State Manager's Accountability Act of 1983 (FISMA) and oversees the activities of internal audit functions within most state agencies. According to state sources, FISMA requires each state agency to maintain effective systems of internal

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<sup>11</sup>In the past, the Federal Highway Administration has reported that there are risks associated with local implementation of federal regulations, including difficulty maintaining compliance with these federal requirements.

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accounting and administrative control, to evaluate the effectiveness of these controls on an ongoing basis, and to review and report biennially on the adequacy of the agency's systems of internal accounting and administrative control. OSAE has not yet determined the scope or approach for its review of Recovery Act funds or the extent to which it can utilize FISMA in assessing compliance with Recovery Act requirements. In addition, the State Controller audits claims for payment submitted by state agencies and provides internal audit services to some state agencies, such as Caltrans, for Recovery Act funds.

The State Auditor, California's independent audit and evaluation office, conducts financial and performance audits as authorized or required by law and requested by the State Legislature. The State Auditor is also annually responsible for conducting California's statewide single audit of numerous federal programs administered in California.<sup>12</sup> Based on the State Auditor's initial analysis of Recovery Act funds the state expects to receive and the formula for determining which programs require an audit, the State Auditor anticipates it will likely need to expand single audit coverage to capture additional programs receiving Recovery Act funds. Finally, on April 3, 2009, the Governor appointed the nation's first Recovery Act Inspector General, whose role is to make sure Recovery Act funds are used as intended and to identify instances of waste, fraud, and abuse.

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**Prior Work of State Auditor Indicates Areas Requiring Additional Oversight**

The most recent single audit, conducted by the State Auditor for fiscal year 2007, identified 81 material weaknesses, 27 of which were associated with programs we reviewed for purposes of this report.<sup>13</sup> The State Auditor plans to use past audit results to target state agencies and programs with a high number and history of problems, including data reliability concerns, and is closely coordinating with us on these efforts. For example, the fiscal year 2007 State Single Audit Report identified eight material weaknesses pertaining to the ESEA Title I program and the Individuals with

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<sup>12</sup>The Single Audit Act of 1984 (Pub. L. No. 98-502) and its 1996 amendments (Pub. L. No. 104-156) require that nonfederal entities that expend a threshold amount each year in federal awards have a single or program-specific audit in accordance with the provisions of the act's audit requirements. OMB Circular A-133 set the threshold amount at \$500,000 or more a year for fiscal years ending after December 31, 2003, and specifies guidance for entities that conduct these single audits.

<sup>13</sup>State of California, *Internal Control and State and Federal Compliance Audit Report for the Fiscal Year Ended June 30, 2007* (June 2008 Report 2007-002).

Disabilities Education Act programs. The audit findings included a material weakness in the California Department of Education's management of cash because it disbursed funds without assurances from LEAs that the time between the receipt and disbursement of federal funds was minimized, contrary to federal guidelines. Education officials told us that they have addressed some of these material weaknesses and, in other cases, they are still working to correct them. If these and other material weaknesses are not corrected, they may affect the state's ability to appropriately manage certain Recovery Act funds. The State Auditor's Office told us that it is in the process of finalizing the fiscal year 2008 State Single Audit Report and plans to issue the report within the next 30 days. In addition, the State Auditor's Office is summarizing the results of the single audit to identify those programs that continue to have material weaknesses. Finally, the State Auditor's Office plans to use the results of other audits it has conducted in conjunction with the single audit to assess risk and develop its approach for determining the state's readiness to receive the large influx of federal funds and comply with the requirement regarding the use of those funds under the Recovery Act.

### State Officials Expressed Concerns about Lack of Guidance and Ability to Measure the Impacts of Recovery Act Funds

State officials with whom we spoke have not yet established plans or processes for assessing the impacts of Recovery Act funds. According to Department of Finance officials, the newly created California Federal Economic Stimulus Task Force will assume this responsibility. Several state agency officials and a local public housing authority believe that additional guidance is needed from the U.S. Office of Management and Budget (OMB) before they can fully address the issue of impact assessments. State officials told us that assessing the impact of Recovery Act funds on job creation in particular will be difficult. That is, while they believe that tracking the impact for contracts, grants, or discrete projects is possible, it is extremely difficult to separate out the specific impact of Recovery Act funds when they are combined with other federal, state, or local funds, as they will be in many situations.

The state program officials with whom we spoke raised a number of specific concerns about their ability to measure the impact of Recovery Act funds. For example,

- California education officials told us they did not yet know how the state will measure the impact of the Recovery Act funds spent on education. The officials said that, although it should be possible to track Recovery Act education spending separately from non-Recovery Act money, this does not mean that they will be able to report on

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specific outcomes that result from this spending. One concern mentioned by several officials is that it may not be possible to link the spending categories used in the accounting system to specific outcomes. Furthermore, even if such links could be made, another difficulty would be determining the extent to which an outcome was the result of the Recovery Act funds received in April 2009 versus the non-Recovery Act funds received earlier in the year for the same program. Finally, officials expressed concern about the incompatibility between desired Recovery Act outcomes and Recovery Act funding. One of the Recovery Act's desired outcomes is job creation and preservation, which requires ongoing funds, but the Recovery Act provides only temporary funds.

- According to Caltrans officials, measuring the full economic impact of highway funds presents challenges. Caltrans officials told us that since Recovery Act funds may be combined with other funds to complete projects, isolating the number of jobs created using just the Recovery Act funds may be difficult. In addition, Caltrans officials told us that guidance on measuring and reporting the effect of Recovery Act funds for transit and fixed-guideway investments has not yet been issued, however they anticipate it will be difficult to report on jobs preserved or created.
- California Employment Development Department officials told us that its existing accounting system can report output, such as how many more participants are registered and enrolled in Workforce Investment Act programs and the level of program services increased due to the Recovery Act. They also said that the existing system can track certain performance indicators for program participants, such as successful employment, wage increases, and job retention. However, these officials noted that they anticipate challenges determining whether such outcomes are specifically due to services supported by the additional Recovery Act funds versus services previously or currently provided to program participants through existing Workforce Investment Act funds.

### California's Comments on This Summary

We provided the Governor of California with a draft of this appendix on April 17, 2009. Members of the California Federal Economic Stimulus Task Force responded for the Governor on April 20, 2009. These officials provided clarifying and technical comments that we incorporated where appropriate.

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## Appendix V: Colorado

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage awards, the State Fiscal Stabilization Fund, and highways.

#### ✓ Medicaid Federal Medical Assistance Percentage (FMAP) Funds

- As of April 3, 2009, the Centers for Medicare & Medicaid Services had made about \$227 million in increased FMAP grant awards to Colorado.
- As of April 16, 2009, the state had not drawn down any of its increased FMAP grant awards.
- State officials noted they are working to ensure that the state is in compliance with Recovery Act provisions governing eligibility for the increased FMAP.

#### ✓ Transportation—Highway Infrastructure Investment

- Colorado was apportioned about \$404 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
- As of April 16, 2009, the U.S. Department of Transportation had obligated \$118.4 million for 19 projects; the Colorado Department of Transportation had advertised 17 of these projects, and 5 of the 17 had been awarded.
- Colorado's Recovery Act transportation funds are being directed to projects that can be advertised within 90 to 180 days of the passage of the act, can be completed within 3 years, and will result in job creation.
- Projects include resurfacing roads and replacing highway bridges in the Denver metropolitan area, as well as improvements to mountain highways.
- Colorado will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.

#### ✓ U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)

- Colorado was allocated about \$509 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
- Before receiving the funds, states are required to submit an application that provides several assurances to the U.S. Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments.
- The Governor is working with the state legislature on a plan for spending the fiscal stabilization funds Colorado will receive to support education. Once legislative concurrence is obtained, the plan will be submitted to the U.S. Department of Education. A state official estimated that could happen as early as the week of April 20, 2009.



Colorado is also receiving additional Recovery Act funds under other programs, such as those under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA), Part B; programs under the Workforce Investment Act; and Edward Byrne Memorial Justice Assistance Grants. These are described throughout this appendix.

**Safeguarding and transparency:** As the state makes its plans, some officials raised concerns about how well the state is positioned to track and oversee Recovery Act expenditures and identified general areas of vulnerability in spending Recovery Act funds. For example, Colorado's accounting system is 18 years old, which will make it challenging for the state to tag and track Recovery Act funds, according to state officials. State officials are determining what approach they will use in tracking funds and told us they currently plan to create an accounting fund to track state agencies' use of Recovery Act funds, employing a centrally defined budget-coding structure to distinguish between Recovery Act and non-Recovery Act federal funds. State officials were also concerned about tracking funds that bypass the state and flow directly to local entities.

**Assessing the effects of spending:** The state is making plans to assess the effects of Recovery Act spending on Colorado's economy. Some agencies plan to use their existing performance indicators to assess the effects of recovery, while others have received guidance including new indicators. Some officials identified concerns with recipients' ability to submit reports more quickly or more frequently than normal, while some questioned how precisely economic effects can be measured.

## Colorado Beginning to Use Recovery Act Funds

Colorado has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible

states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 3, 2009, CMS had made about \$227 million in increased FMAP grant awards to Colorado. As of April 16, 2009, state officials had not drawn down any of the state's increased FMAP grant awards. State officials noted they are working to ensure that the state is in compliance with Recovery Act provisions governing eligibility for the increased FMAP. Officials also indicated that, in order to account for the increased FMAP funds available through the Recovery Act, the state has created unique codes that will calculate the additional federal reimbursement. The state will use these codes to assist with the proper drawing down and reporting of these expenditures on quarterly Medicaid reports.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and to undertake other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the Governor must certify that the state will maintain its current level of transportation spending, and the Governor or other appropriate chief executive must certify that the state

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

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or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Colorado provided this certification but noted that the state's level of funding was based on "planned nonbond state expenditures" and represented the best information available at the time of the state's certification.<sup>3</sup>

Colorado was apportioned about \$404 million in Highway Infrastructure Investment Recovery Act funds by the U.S. Department of Transportation on March 2, 2009. As of April 16, 2009, the U.S. Department of Transportation had obligated \$118.4 million for 19 Colorado projects.<sup>4</sup> Seventeen of these projects, which include resurfacing roads and replacing highway bridges in the Denver metropolitan area and improvements to mountain highways, had been advertised for bid, and 5 of the 17 projects had been awarded. According to Colorado Department of Transportation officials, the department has a well-established process for distributing funds and contracting projects and has already begun to use this process in applying for Recovery Act funds. In order to spend funds quickly and create jobs, Colorado is directing Recovery Act transportation funds to projects that can be advertised within 90 to 180 days of the passage of the Recovery Act, can be completed within 3 years, and will result in job creation. Department officials told us they are emphasizing construction projects rather than projects in planning or design phases, in order to maximize job creation.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures it will take action to meet certain educational requirements such as increasing teacher

<sup>3</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>4</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

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effectiveness and addressing inequities in the distribution of highly qualified teachers.

The Governor has proposed a plan for spending the majority of the \$760 million in stabilization funds Colorado will receive to support education, focusing on offsetting current and planned reductions in state funding for higher education. Officials told us that funding cuts were directed primarily toward higher education rather than kindergarten through 12th grade education because of a state constitutional provision requiring guaranteed annual increases in state funding of kindergarten through 12th grade education<sup>6</sup>—and as a result, SFSF funds are more urgently needed in higher education. The state will receive its first allocation of funds—\$509 million or 67 percent of the total—after it has applied to Education, which it plans to do once the Governor's office and legislature agree on the plan and the state's budget. As of April 20, 2009, the state's General Assembly was negotiating the final budget and a school finance bill that could affect the specific use of the SFSF funds. A Colorado official said that if the state approves a budget the week of April 20, 2009, the proposal could go to Education soon after that date. The Governor is also developing a plan for the Government Services Fund, a component of the SFSF, which will provide \$138 million of SFSF funds that may be used for public safety and other government services.

**Colorado Will Manage  
Recovery Act Funds  
through an Oversight  
Board and State Executive  
Departments**

Following passage of the Recovery Act, Colorado's Governor established an oversight board, the Colorado Economic Recovery Accountability Board, to oversee Colorado's Recovery Act funding and ensure funds are spent effectively and transparently. The board is chaired by the Director of the Colorado Office of Economic Development, who has also been charged with being Colorado's recovery coordinator. The board is composed of 12 public- and private-sector leaders from across the state, including the state treasurer, a state senator and a state representative, and a number of business leaders. To date, the board has held three public meetings during which members discussed the short time frames for disbursing Recovery Act funds and a lack of federal guidance, among

<sup>6</sup>According to a Colorado state legislative study, in 2000, Colorado voters approved a measure to increase education spending in the state; this amendment directed a portion of state tax revenues to the State Education Fund through fiscal year 2011. The amendment requires an annual increase in per pupil funding and requires the state general fund appropriation for state aid to schools to increase by 5 percent per year, unless state personal income increased by less than 4.5 percent during the previous year.

other issues. The board has also developed a Web site to publicize information about the Recovery Act.<sup>6</sup>

Management of and decisions about Recovery Act funds are the responsibility of the Governor, according to state officials. The Governor's office is directly responsible for exercising discretion with regard to certain funds such as portions of the SFSF. The Governor is working in consultation with the executive directors of Colorado's state departments and agencies to develop plans for spending Recovery Act funds, which are to be publicly available on the state's Web site. Officials told us the Governor has directed that all departmental decisions on spending Recovery Act funds are to be made in line with the original charge of the Recovery Act to promote job creation or preservation and economic development, as well as the Governor's agenda. The decision process for using Recovery Act funds depends on the program, consistent with federal and state statutes and guidance. Officials from several departments, such as the Departments of Public Safety, Labor and Employment, and Local Affairs, told us they have made initial programmatic decisions for Recovery Act funds. Other programs have not made such decisions; for example, Colorado Department of Education officials told us the department will distribute funds such as those under the ESEA and IDEA programs directly to local school districts to make programmatic decisions about the funds.

Many Colorado officials said the Recovery Act would increase their departments' workloads and said they would like to add personnel and perhaps systems to manage the funds, but the overall extent to which Recovery Act funds are permitted to be used for those costs is uncertain. While some officials we interviewed said their departments had received or would receive Recovery Act funds to cover administrative or management activities, officials in other departments did not know whether they would receive funds for that purpose. Officials at the Colorado Department of Labor and Employment, for example, said they can spend about \$1.5 million in Recovery Act funding to cover

<sup>6</sup>Colorado's Recovery Act Web site is <http://www.colorado.gov/recovery/>. To help inform the public about the results of Recovery Act spending in Colorado, the state also plans to create a Web-based map of projects receiving Recovery Act funds and plans to "brand" projects funded by the Recovery Act, where possible. For example, the Colorado Department of Transportation has already developed a sign template for road projects funded by the Recovery Act.

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administrative costs associated with Workforce Investment Act programs,<sup>7</sup> consistent with their normal procedures for administration of the programs, while officials from the Colorado Department of Education said they were uncertain what, if any, funds they were going to receive to administer and manage recovery programs. State officials told us they believe the government services portion of the SFSF can be used by the Colorado Department of Education and other state departments to cover administrative costs.<sup>8</sup>

### Colorado Officials Expressed Concerns Related to Tracking of, Internal Controls over, and Safeguards for Recovery Act Funds

Colorado officials identified general areas of vulnerability in spending Recovery Act funds, as well as specific concerns about their ability to oversee Recovery Act funds coming into the state. Areas of vulnerability include new programs and localities that may be ill-equipped to manage the influx of new funds. In addition, state officials are concerned about their ability to oversee Recovery Act funds because of three primary challenges: (1) the state's accounting system is 18 years old, which may make it challenging to tag and track Recovery Act funds; (2) adequate resources to administer and audit expenditures of Recovery Act funds may not be available; and (3) state officials are still determining what they will be required to track and report on and are particularly concerned about tracking funds that bypass the state and flow directly to local entities.

### Colorado Officials Identified Potential Areas of Vulnerability in Spending Recovery Act Funds

The state's departments have begun to identify potential areas of vulnerability in spending Recovery Act funds, according to officials. One area that officials identified is the influx of new Recovery Act funds that must be adequately managed as they are spent quickly. For example, some programs, such as Medicaid, already have known weaknesses in managing existing funds (identified, for example, in audits conducted by the Colorado state auditor) and may be challenged in managing large amounts of additional funds. A second vulnerable area, according to officials, involves new programs that do not have well-established processes, or programs that will need to establish additional processes, to accommodate

<sup>7</sup>In addition, an official from the department said that regions within the state that receive Recovery Act funds for Workforce Investment Act programs can also use 10 percent of their regional allocations for administration.

<sup>8</sup>In April 2009, the U.S. Department of Education issued guidance on the SFSF, stating that administrative costs associated with implementing the Recovery Act are allowable expenditures under the SFSF.

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significant funding increases, such as the state's energy program, which will receive funds for weatherization and other energy projects. Funds that go directly to localities are a third area that may be vulnerable because, according to officials, the state does not currently oversee these funds and cannot provide assistance to local entities, some of which may not be well-equipped to manage the increased funds.

#### Colorado's Accounting System Is Outdated

State officials were concerned that Colorado's accounting system—the Colorado Financial Reporting System (COFRS)—is 18 years old, which may make it difficult for the state to use and track Recovery Act funds. For example, state officials are concerned about Colorado's ability to report quickly on Recovery Act expenditures. Because of limitations associated with COFRS, officials told us the state will have difficulties meeting reporting requirements established for certain Recovery Act expenditures, such as the requirement in section 1512 of Title I, Division A of the Recovery Act calling for recipient reports within 10 days of the end of the calendar quarter. In addition, some individual state departments do not use the COFRS grant module and therefore must manually post aggregate revenue and expenditure data to COFRS. Consequently, given the state's current capabilities, data on total Recovery Act funding received by the state may not be able to be drawn from COFRS and may have to be compiled through a manual exercise outside of the central financial management system, raising internal control concerns among some officials we talked with. These concerns include inadequate audit documentation on how the information is compiled, potential human error in inputting and aggregating information, and potentially inconsistent or duplicative reporting from various agencies on the extent and nature of Recovery Act funding received and used. Finally, state officials also voiced concerns that COFRS uses Catalog of Federal Domestic Assistance numbers to track grants from each federal agency, but some federal departments are not establishing unique Catalog of Federal Domestic Assistance numbers for some Recovery Act funds, which will make automated reporting difficult.

#### Procurement and Audit Resources May Be Inadequate

Officials with the Colorado Department of Personnel & Administration were concerned that vacancies in procurement positions posed an impediment to effective tracking and control over the state's Recovery Act funds. Many Colorado state agencies have vacancies for procurement officers, which have been left unfilled due to the state budget shortfall and a consequent hiring freeze. For example, the Department of Personnel & Administration, which administers statewide contracts and supports

several state agencies that have little or no purchasing authority, currently has three vacancies in its purchasing agent and contracting positions. Filling these vacancies would enable this department to better assist state agencies receiving Recovery Act funds, according to department officials. Similar purchasing agent vacancies exist, according to these officials, in the Colorado Departments of Corrections, Education, Human Services, Labor and Employment, and Local Affairs. Colorado Department of Personnel & Administration officials hope to hire former or retired state employees with procurement experience on a 6-month basis to alleviate this problem, but additional funding—and possibly legislative and budgetary approval—may be needed in order to hire temporary procurement personnel, which could potentially delay hiring if the state needs to await legislative action.

State officials were also concerned with the amount of audit coverage throughout the state. For example, officials with the Colorado state auditor's office told us their office would have difficulty absorbing additional work associated with the Recovery Act, and believed that state oversight capacity was limited. For example, according to these officials, the Department of Health Care Policy and Financing (the state's Medicaid agency) has had three controllers in the past 4 years; these officials also told us the state legislature's Joint Budget Committee recently cut field audit staff levels for the state Department of Human Services in half. Officials with the Department of Personnel & Administration told us their department's internal auditor position is vacant, while officials with the Colorado Department of Transportation told us that two of their department's financial management positions, including the deputy controller position, are vacant. At the county level, Jefferson County recently terminated its internal auditor and eliminated its internal control audit office.

The reduced number of staff in oversight positions resulted in part from budget cuts and staffing decisions during the state's last economic downturn, and state officials told us certain positions would be difficult to fill because of the state's current hiring freeze. Officials said because the "ratchet effect" of Colorado's constitutional and legislative requirements limits the growth of spending, it can be difficult to re-establish and fill



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positions that are eliminated during economic downturns.<sup>9</sup> Officials told us, for example, that some state agencies have not refilled all of the staff positions they lost to budget cuts during Colorado's 2001-2003 downturn.

### Colorado Officials Are Still Determining State Reporting Requirements

Colorado officials said they have not received state-specific guidance on Recovery Act reporting from the federal Office of Management and Budget. They said the guidance provided in February and April 2009 was addressed to federal departments and agencies, and it was necessary to determine whether and how this guidance applied to state governments. Officials wondered, for example, whether the state would be required to report centrally on all funds coming through the state or whether state agencies will report as normal through federal departments, or both; what the frequency and form of reports will be; and the level to which funds will need to be tracked and reported (e.g., at the recipient level, subrecipient level, etc.). Officials were especially concerned that a substantial portion of funds provided to Colorado will go directly to local entities, making it difficult for state officials to be aware of and track all funds within the state.

In the absence of state-specific guidance, state officials were taking some steps on their own to track the use of Recovery Act funds. Department of Personnel & Administration officials said they anticipated that statewide reporting on the use of Recovery Act funds will be necessary, in addition to having individual state departments and agencies reporting directly to their respective federal granting agencies. The department discussed various tracking and reporting methodologies with state department controllers to determine what tracking method would be the most effective and least disruptive; the department determined that the state would create an accounting fund through which it could track state agencies' use of Recovery Act funds and would employ a centrally defined budget-coding structure for Recovery Act funds, which should be able to distinguish between Recovery Act funds and other federal non-Recovery

<sup>9</sup>The provisions include the Taxpayer Bill of Rights, or TABOR, which the voters passed in 1992. These provisions, as described by state officials and documents, limit annual growth in state revenues to the amount of population growth plus inflation over the previous year, and also require any tax increase to be voted on by taxpayers. The amendment is also considered to have "locked in" a separate 6-percent limit on state spending increases passed by the legislature in 1991. During an economic downturn, reduced government revenues may lead to reduced government services and expenditures. The "ratchet effect" comes into play during subsequent recovery periods, when constitutional revenue and spending limitations restrict the growth of these services.

Act funds. This accounting process would capture only those funds flowing through state agencies. State officials said they are still determining how they will capture funds that do not flow through the state and said that guidance will be important in order to prevent duplicate reporting of Recovery Act funds by state and federal agencies. Although they are moving forward, state officials are hesitant to establish statewide reporting requirements for fear they could waste state resources developing and implementing an approach that is not consistent with the federal guidance ultimately established.

### Colorado Is Developing Plans to Assess the Effects of Recovery Act Funds

Colorado's state departments with responsibility for the funds we examined described a range of approaches to assess and report on the effects of recovery spending in the state. Some agencies plan to use their existing performance indicators to assess the effects of Recovery Act funding, as they have not yet received reporting guidance from the federal departments involved. For example, Colorado Housing and Finance Authority officials said they plan to use existing indicators, such as the number of affordable housing units created and the relative income levels of populations served by those units, to assess the effects of Recovery Act funding for the Low-Income Housing Tax Credit. Other agencies, such as the Colorado Department of Transportation, have received guidance to report on existing and new indicators, such as direct jobs associated with Recovery Act projects; the indicators will involve a significant increase in data collection and reporting by the department, including gathering data from more entities and reporting more frequently than the department has reported in the past, according to department officials. In another example, the Colorado Department of Public Safety, which did not report on jobs in the past, will report on the jobs created or retained with the spending of justice assistance grants. In addition, it will report on a set of new performance measures being developed by the federal Department of Justice Bureau of Justice Assistance. Department of Public Safety officials are concerned about the timing of reporting job creation and retention data, however, because the Recovery Act requires states to report 10 calendar days after the end of each quarter, which is faster than the normal reporting time frames and, according to officials, will necessitate that recipients report to the department within 5 calendar days of the end of the quarter. Some grantees will have difficulty reporting within such short time frames, according to one department official, because they still mail or hand deliver their reports.

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Appendix V: Colorado

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State and local officials raised other concerns about tracking the economic effects of Recovery Act funds. Officials with the state auditor's office, for example, said that tying specific funding to the creation of particular jobs is problematic. One state official pointed out that increased FMAP available under the Recovery Act would reduce the amount of funds that Colorado will need to spend on its Medicaid program, allowing the state to use these funds for other purposes and avoid cutting other programs to balance the state budget. However, because specific program cuts were not determined, identifying the preserved programs and their economic effects is impossible. While some state departments have received guidance on counting jobs created or retained, officials from at least one local department said they needed more guidance about how to measure the number of new jobs created. Another official said that her department will report jobs created or retained but questioned how indirect jobs would be counted. According to this official, spending Recovery Act funds to purchase items such as equipment or vehicles will have substantial economic effects, particularly the creation of indirect jobs, but she was not certain how these jobs would be counted and asked whether clarification would come through Office of Management and Budget or other guidance. To measure such impacts for the state, an economic impact assessment would need to be conducted, according to a member of the Colorado Economic Recovery Accountability Board. The board is considering contracting for such an assessment, according to the member, but has not yet decided on whether or when to do it.

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**Colorado's Comments  
on This Summary**

We provided the Governor of Colorado with a draft of this appendix on April 17, 2009. State officials from the Governor's office responded for the Governor on April 20, 2009. In general, they agreed with this summary of Colorado's recovery efforts to date. The officials also provided technical comments that were incorporated, as appropriate.

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**Staff  
Acknowledgments**

In addition to the contacts named above, Steve Gaty, Susan Iott, Tony Padilla, Ellen Phelps Ranen, Lesley Rinner, Glenn Slocum, and Mary Welch made significant contributions to this report.

## Appendix VI: Florida

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$1.4 billion in increased FMAP grant awards to Florida.
  - As of April 1, 2009, Florida has drawn \$817 million, or 58.6 percent of its increased FMAP grant awards to date.
  - From January 2008 to January 2009, the state's Medicaid enrollment increased from 2,151,917 to 2,391,569, with most enrollment changes attributable to two population groups: (1) children and families and (2) other individuals, including those with disabilities.
  - While funds are made available as a result of the increased FMAP, the state legislature is still determining how to make use of these funds.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Florida was apportioned about \$1.3 billion for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had not obligated any Recovery Act funds for Florida projects.
  - On April 1, 2009, the Florida Department of Transportation (FDOT) prepared a final listing of potential Recovery Act funded projects and on April 15, 2009, the Florida Legislative Budget Commission approved the list of projects. The U.S. Department of Transportation, Federal Highway Administration must also approve the final listing of projects before the state can advertise bids for contracts.
  - These projects include activities such as resurfacing roads, expanding existing highways, repairing bridges and installing sidewalks.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Florida was allocated about \$1.8 billion from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance-of-effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. According to Florida officials, Florida plans to apply for a waiver to obtain these funds after the Department of Education issues final instructions for waiver applications.

Florida is also receiving Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA); and Workforce Investment Act employment and training programs. The status of plans for using these funds is described throughout this appendix.

**Safeguarding and transparency:** The Governor has created the Florida Office of Economic Recovery to oversee, track and provide transparency in how Recovery Act funds are spent. In addition, according to Florida officials, Florida's accounting system will be able to separately track the Recovery Act funds flowing through the state government. Florida plans to publicly report its Recovery Act spending on a state Web site. Florida state accountability organizations have identified areas where Recovery Act funds may be at greater risk of fraud, waste, and abuse, such as Medicaid, and have begun to collaborate in developing plans for oversight.

**Assessing the effects of spending:** Florida state officials are in the early stages of developing plans to assess the effects of Recovery Act spending and told us that guidance from the federal government would be instrumental in developing their plans. On April 3, 2009, the U.S. Office of Management and Budget (OMB) issued guidance indicating that it will be developing a comprehensive system to collect information, including jobs retained and created, on Recovery Act funds sent to all recipients. Florida state officials told us that they will ask OMB to allow the state to obtain data from this system on local entities in Florida that receive Recovery Act funds directly from federal agencies.

## Florida Beginning to Use Recovery Act Funds

Florida has begun to use some of its funds made available as a result of the Recovery Act, as follows:

**Increased Federal Medicaid Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal

matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008 and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provide for: (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that the state must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, Florida has drawn down \$817 million in increased FMAP grant awards, which is about 58.6 percent of its awards to date.<sup>3</sup> The state is determining how to make use of the state funds made available as a result of the increased FMAP grant awards. Officials told us that each state agency with a budget impact resulting from Recovery Act funding has prepared budget amendments for the current state fiscal year (July 1, 2008, to June 30, 2009) for consideration by the Executive Office of the Governor and the Legislative Budget Commission (LBC). On April 15, 2009, the LBC approved 17 amendments to the 2008-2009 state appropriation to authorize the use of Recovery Act funds. The state has drawn down funds that are for Medicaid expenditures retroactive to October 1, 2008. Florida officials told us they require additional guidance from CMS on the prompt payment requirements, and for CMS to provide

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP grant awards for Medicaid service expenditures made on or after October 1, 2008.

<sup>3</sup>Florida received increased FMAP grant awards of \$1.4 billion for the first three quarters of federal fiscal year 2009.

the state guidance, if applicable, on any additional reporting requirements.<sup>4</sup>

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Florida provided this certification, but conditioned it, noting that state funding for the transportation programs is provided from dedicated funding sources that are subject to fluctuations resulting from economic conditions.<sup>6</sup>

On April 15, 2009, the Florida LBC approved the Recovery Act funded projects that the FDOT had submitted. As of April 16, 2009, the U.S. Department of Transportation had not obligated any Recovery Act funds for Florida projects.<sup>5</sup> The Federal Highway Administration must approve this final listing of projects before the FDOT can advertise bids or request reimbursement from the Federal Highway Administration. The state's projects include activities such as resurfacing roads, expanding existing highways, repairing bridges, and installing sidewalks.

<sup>4</sup>Under the Recovery Act, to be eligible for the increased FMAP grant awards, states must comply with prompt payment requirements that require states to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt.

<sup>5</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>6</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers. Florida's initial SFSF allocation is about \$1.8 billion. However, according to Florida officials, the state will not be able to meet the maintenance-of-effort requirement to readily qualify for these funds because revenue declines led to cuts in the state's education budget in recent years. The state will apply to Education for a waiver from this requirement; however, they are awaiting final instructions from Education on submission of the waiver. Florida plans to use SFSF funds to reduce the impact of any further cuts that may be needed in the state's education budget.

### Florida's Planning Process Has Set the Stage for Decisions on Spending of Recovery Act Funds

Florida state officials began preparing for the use of Recovery Act funds prior to the receipt of the funds. Florida officials believe that Recovery Act funds are critical to addressing the state's budgetary crisis and maintain necessary services to its citizens. According to state officials, the state plans to use about \$3 billion of Recovery Act funds to reduce the state's \$6 billion budget shortfall for state fiscal year 2009-2010. One reason for this shortfall is the significant declines in revenue Florida has faced in recent years—23 percent since state fiscal year 2005-2006, from about \$27.1 billion to \$20.9 billion in state fiscal year 2008-2009—due to such factors as the recession and housing crisis. State officials estimate that Florida will receive about \$15 billion in Recovery Act funds over 3 state fiscal years. Florida estimates that approximately \$14.1 billion of this amount will flow through state agencies, with at least \$4.7 billion of this amount allocated to local entities. In addition, approximately \$1.2 billion in funding will be directly allocated to local entities from federal agencies.

On March 3, 2009, the Governor established the Florida Office of Economic Recovery that is responsible for overseeing, tracking and providing transparency of Florida's Recovery Act funds. The office is headed by the Special Advisor to the Governor for the Implementation of the American Recovery and Reinvestment Act (Recovery Czar) and includes three other staff members on loan from state agencies. The Florida Office of Economic Recovery also established an implementation team that meets twice a week and includes representatives from each of



the state's program agencies and administrative offices, such as the Office of Policy and Budget, the Chief Inspector General, the State Auditor General, the Department of Financial Services, as well as representatives from the Florida Association of Counties and the Florida League of Cities. On March 17, 2009, pursuant to Section 1607 of division A, title XVI of the Recovery Act, the Governor certified that the state would request and use funds provided by the act. Additional certifications for transportation, energy, and unemployment compensation have also been submitted.

According to state officials, before Florida agencies can use the Recovery Act funds, the Florida legislature must authorize the use of all funds received by state agencies, including those passed-through to local governments. On April 15, 2009, the joint Legislative Budget Commission met and approved 17 amendments to the 2008-2009 state budget authorizing appropriations totaling almost \$4 billion in Recovery Act funds. The Florida state legislature is still in session and developing the state's fiscal year 2009-2010 budget. As explained by state officials, if the legislature does not pass the authorization for the Recovery Act funds before the end of the session (May 1, 2009), a joint legislative budget committee can later amend the Appropriation Act and authorize the use of the Recovery Act funds or the legislature can reconvene.

To promote transparency, the Florida Office of Economic Recovery implemented a state Recovery Act Web site that became operational on March 19, 2009.<sup>7</sup> The Web site is intended to provide information to the public on the amount and uses of Recovery Act funds the state receives and on resources being made available to citizens, such as unemployment compensation and workforce training.

#### Florida Has a System to Track Recovery Act Funds but Anticipates Challenges in Obtaining Timely Data from Localities

Officials from Florida's Department of Financial Services said that the state's accounting system—Florida Accounting Information Resource (FLAIR)—will be used to track Recovery Act funds that will flow through the state government. The state agencies will record the Recovery Act funds separately from other state and federal funds using selected identifiers in FLAIR such as grant number or project number. Officials in some Florida state program agencies raised concerns that local areas will not be able to provide timely data to enable state agencies to meet financial reporting deadlines for the quarterly reports required by the

<sup>7</sup>[www.flarecovery.com](http://www.flarecovery.com)

## Appendix VI: Florida

Recovery Act. These reports on the uses of Recovery Act funds are due 10 days after the end of each quarter.<sup>8</sup> In addition, Florida officials and a group representing local school superintendents were particularly concerned about the ability of school districts to meet these deadlines after having experienced reductions in administrative staff due to recent budget cuts.

Florida officials submitted feedback to OMB suggesting that OMB consider providing guidance on reconciling the information provided in the Recovery Act quarterly reports with other federal reporting requirements to avoid confusion. According to Florida officials, quarterly reports on many federal grants are due 45 days after the end of the quarter and reporting systems are currently oriented towards these requirements. Florida officials added that it is likely that meeting the Recovery Act quarterly reporting requirement will necessitate the submission of preliminary reports.

**State Agencies Are  
Providing Guidance to  
Localities on Use of Funds**

Some state agencies have issued or are developing guidance to assist local areas in planning for the use of Recovery Act funds that will be passed through the state to local areas. For example, on April 1, 2009, Florida received about \$580 million for Title I, Part A of ESEA and for IDEA, which will be passed through to local school districts. In anticipation of these funds, the Florida Department of Education provided guidance to school districts on strategies for using education funds, such as assigning high-performing teachers to low-performing schools, providing reading coaches to schools, and investing in intensive professional development for teachers.

On March 19, 2009, Florida received almost \$143 million for the Workforce Investment Act Adult, Youth, and Dislocated Worker employment and training programs and made \$121 million available to regional workforce areas the next day. As of April 13, 2009, regional workforce areas had drawn down about \$744,000 of these funds, according to a Florida official. Florida's Agency for Workforce Innovation had previously established various task teams, composed of state and regional workforce officials that created action plans for implementing these funds. For example, to facilitate the rapid expansion of summer youth employment programs, the

<sup>8</sup>Recovery Act, div. A, title XV, § 1512(c).

state plans to develop a local implementation checklist and a toolkit of summer youth materials.

### Plans for Safeguards and Controls Being Developed at State Level

Florida has various oversight entities responsible for monitoring, tracking, and overseeing financial expenditures, assessing internal controls and ensuring compliance with state and federal laws and regulations: the Office of the Chief Inspector General, Auditor General, Office of Program Policy Analysis and Government Accountability (OPPAGA), and the Department of Financial Services. Each state agency has an Office of Inspector General (OIG) that is responsible for conducting audits, investigations, and technical assistance, and promoting accountability, integrity and efficiency in the state government. The Auditor General has broad audit authority with respect to audits of government agencies in Florida and routinely conducts Single Audits of the State of Florida reporting entities and of the state's district school boards. The single audits include determining if federal and state expenditures are in compliance with applicable laws and regulations and assessing the effectiveness of key internal controls. Florida's OPPAGA—the research unit of the state's legislature—is responsible for conducting studies on the performance of state agencies and programs to identify ways to improve services and cut costs. In addition, the Florida Department of Financial Services is responsible for overseeing state expenditures and financial reporting. Independent certified public accountants also conduct annual financial audits of local governmental entities, such as counties and municipalities. According to state officials, Florida law requires that the scope of such audits encompass federal and state Single Audit requirements, as applicable.

### Potential Areas of Vulnerability with Florida Recovery Act Funds

Past experience has highlighted financial management vulnerabilities in agencies that will receive Recovery Act funds. Auditor General and state OIG reports identified several high-risk areas that are vulnerable to fraud, waste, and abuse. For example, in 2008:

- State officials identified Medicaid as the highest risk program. The Auditor General reported breakdowns in internal controls over the Medicaid program because state Medicaid program officials failed to properly document and verify recipients' income, which increased the risk of ineligible individuals receiving program benefits.

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- The Auditor General reported that, for some federal programs, the Florida Department of Education failed to provide monitoring that reasonably ensured sub-recipient adherence to program requirements.
- The Auditor General reported that the Florida Department of Community Affairs failed to provide information that was needed to assess the success or progress of its federal low-income housing community development block grant program.
- The agency OIGs continue to provide oversight through audits and investigations of contracting and grant activities associated with federal funds. For instance, FDOT and Florida's Department of Education OIG reported on contractors' inaccurate reporting of expenditures and inadequate oversight of sub-contractors. Moreover, in July 2008, the FDOT OIG reported their review of contract files disclosed that differences between the state's accounting system payments and the recipient expenditures were not adequately explained.

State officials also expressed some broader concerns about other potential risks. For example, state officials identified new programs in the Recovery Act as potentially risky and noted that the state's fiscal year 2009 Single Audit report that will cover such new programs will not be completed until spring 2010. State officials also expressed concern about potential risk in programs receiving large funding increases under the Recovery Act. For example, Florida Department of Law Enforcement officials stated that the amount of Recovery Act funds received for the Edward Byrne Memorial Justice Assistance Grant Program, which is designed to help prevent and control crime and improve the operations of the criminal justice system will be four to five times the amounts received in prior years. For these programs, they estimate that about \$52 million will be passed through to 67 local Florida counties, which have had grants collectively totaling only \$12 million to \$15 million in past years.

#### Plans for Oversight of Florida Recovery Act Funds

In response to the Recovery Act, Florida's Chief Inspector General established an enterprisewide working group of agency OIG's to evaluate risk assessments, and promote fraud prevention, awareness, and training. The group members are updating their annual work plans by including the Recovery Act funds in their risk assessments and will leave flexibility in their plans to address issues related to these funds. In preparing to conduct the Single Audits for 2008-2009 and subsequent fiscal years, the Auditor General is monitoring the state's plans for accounting for and

expending Recovery Act funds, tracking the expected changes in OMB's Single Audit requirements, and participating in the National State Auditors Association's efforts to provide input on Recovery Act accounting, reporting, and auditing issues. The Auditor General expects the number of major federal programs to increase as a result of the large infusion of Recovery Act funds into the state, thus increasing the number of federal programs that the Auditor General must audit as part of the state's annual Single Audit. Officials from Florida's OPPAGA expect an increase in the number of legislative requests for their studies—particularly those focused on education programs—as Recovery Act funds are disbursed to recipients.

The OIGs are developing and refining strategies to ensure oversight of Recovery Act funds. For example, the FDOT OIG is developing plans to increase its up-front monitoring activities for transportation funds to mitigate the potential risk of fraud, waste, and abuse. Some of these activities include:

- Designating a team of seven auditors to monitor Recovery Act expenditures and other related activities;
- Developing fraud awareness training specifically for Recovery Act projects;
- Conducting risk assessments of Recovery Act transportation projects; and
- Monitoring and providing oversight for the pre-construction, advertisement, bid, award, and contract-letting activities for Recovery Act projects.

Florida officials told us that separate accounts have been established for receipt of increased FMAP grant awards. The OIG in the Agency for Health Care Administration will follow established recovery protocol and processes to prevent and detect Medicaid overpayments by conducting detection analyses and audits, imposing sanctions, and making referrals to the Medicaid Fraud Control Unit and other regulatory and investigative agencies as appropriate.

According to Florida state officials, the state completed an initiative to strengthen contracting requirements several years ago. For example, the majority of state contracts greater than \$1 million are required to be reviewed for certain criteria by the Department of Financial Services'

## Appendix VI: Florida

Division of Accounting and Auditing before the first payment is processed. The contract must also be negotiated by a contract manager certified by the Florida Department of Management Services, Division of State Purchasing Training and Certification Program.

#### Availability of Resources for Oversight

In light of decreased state budgets that have resulted in prior staff reductions, Florida state auditing officials expressed concern about the adequacy of staff resources to provide oversight of Recovery Act funds beyond that required under existing federal Single Audit Act requirements. For example, the Auditor General told us that the office has not hired new staff for over a year and about 10 percent of the office's positions remain unfilled. In addition, OPPAGA officials told us their staff has decreased by 10 percent in the past 2 years. State officials told us that the efficient use of existing and projected resource levels will require an ongoing assessment of risks and priorities and the allocation of staff resources to ensure the required oversight of state and federal funds, including Recovery Act funds.

#### Plans to Assess Impact of Recovery Act Funds Are in Initial Stages

Florida state agencies were in the early stages of developing plans to assess the effects of the Recovery Act spending because they were waiting for guidance from OMB on how to measure jobs retained and created with Recovery Act funds. For example, Florida Department of Law Enforcement (FDLE) officials said that they could count the number of staff hired to implement a new program, but they did not know how to count the number of jobs retained or created if Recovery Act funds are used for purchases of goods such as new police cruisers. In addition, FDLE and other state officials said they needed clear OMB guidance in order to build this information upfront into the data reporting requirements. Florida's Department of Education has created a new form that school districts will use to report quarterly Recovery Act expenditures and the number of jobs retained and created, but they need additional guidance from OMB to develop instructions for school districts on how to count these jobs.

Florida's Agency for Workforce Innovation is encouraging recipients of Recovery Act funds throughout the state to list jobs created with the funds in the state's existing online job bank. By including tags in the system to identify the jobs linked to Recovery Act funds, the agency expects to be able to count specific jobs created with the funds. A local workforce investment board official told us that the board is publicizing the use of

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the job bank for Recovery Act jobs through radio and town hall appearances and mailings to potential recipients of Recovery Act funds.

Because Florida is only required to collect data on jobs created with Recovery Act funds for which Florida is the recipient, Florida officials plan to include data on the state Recovery Act Web site on all jobs created with Recovery Act funds in Florida. On April 3, 2009, OMB issued guidance indicating that it will be developing a comprehensive system to collect information, including jobs retained and created, from all recipients of Recovery Act funds. The state plans to ask OMB if they can obtain data relevant to Florida collected by the national reporting system on jobs retained and created with Recovery Act funds. According to Florida officials, this will reduce duplication and increase the efficiency of their reporting.

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**Florida's Comments  
on This Summary**

We provided the Governor of Florida with a draft of this appendix on April 17, 2009. The Special Advisor to Governor Charlie Christ, Florida Office of Economic Recovery, responded for the Governor on April 20, 2009. In general, the Florida official concurred with the information in the appendix. The official also provided technical suggestions that were incorporated, as appropriate.

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**Staff  
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In addition to the contacts named above, Fannie Bivins, Carmen Harris, Kathy Peyman, Robyn Trotter, and Cherie' Starck made major contributions to this report.

## Appendix VII: Georgia

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$521 million in increased FMAP grant awards to Georgia.
  - As of April 1, 2009, Georgia had drawn down about \$312 million, or 60 percent of its initial increased FMAP grant awards.
  - State officials plan to use funds made available as a result of the increased FMAP to address increased caseloads, offset general fund needs, and maintain current benefit levels and provider reimbursement rates in the state's Medicaid program.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Georgia was apportioned about \$932 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had not obligated any Recovery Act funds for Georgia projects.
  - On April 7, 2009, the Governor certified that the Georgia Department of Transportation plans to spend \$208 million on 67 projects throughout the state. The department plans to award contracts for most of these projects by May 22, 2009.
  - These projects include maintenance, bridge work, and other activities.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Georgia was allocated about \$1 billion from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. Georgia plans to submit its application in late April or early May.
  - The state's fiscal year 2010 budget, which passed on April 3, 2009, included \$521 million in state fiscal stabilization funds for education.



Georgia also is receiving Recovery Act funds under other programs, such as Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); the Individuals with Disabilities Education Act, Part B; and the Tax Credit Assistance Program. The status of plans for using these funds is discussed throughout this appendix.

**Safeguarding and transparency:** A small core team consisting of representatives from the Office of Planning and Budget, State Accounting Office, and Department of Administrative Services (the department responsible for procurement) is taking steps to establish safeguards for Recovery Act funds and mitigate identified areas of risk. For example, the State Accounting Office has issued guidance on tracking Recovery Act funds separately, and the Office of Planning and Budget is developing a state-level strategy to monitor high-risk agencies. The State Auditor and Inspector General will monitor the use of Recovery Act funds.

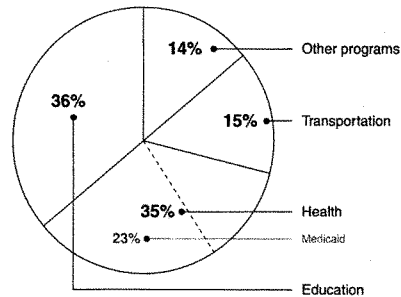
**Assessing the effects of spending:** While waiting for additional federal guidance, the state has taken some steps to assess the impact of Recovery Act funds on the state, including adapting an automated system currently used for financial management to meet Recovery Act reporting requirements.

### Georgia Beginning to Use Recovery Act Funds

Although Georgia is still awaiting final information from the federal government, the state estimates it will receive about \$7.3 billion in funding under the Recovery Act. Of that amount, about \$467 million (or 6 percent) will be awarded by federal agencies directly to localities and other nonstate entities. As shown in figure 5, the majority of Recovery Act funds will support education (36 percent), health programs (35 percent, of which 23 percent will go toward Medicaid), and transportation (15 percent). The Governor completed the blanket certification for Recovery Act funds on March 25, 2009, confirming that the state will use the funds to create jobs and promote economic growth.<sup>1</sup>

<sup>1</sup>As of April 17, 2009, the Governor had also completed certifications for an arts program, energy efficiency, transportation, and unemployment insurance.

**Figure 5: Georgia's Estimated Recovery Act Funding, by Major Programs, as of April 17, 2009**



Source: Georgia Office of Planning and Budget.

Note: Other programs include those for housing, energy, and employment and training. The Office of Planning and Budget estimates are based on federal announcements and estimates from Federal Funds Information for States. The primary mission of Federal Funds Information for States is to track and report on the fiscal impact of federal budget and policy decisions on state budgets and programs.

The state has begun to use or plans to use funds for the following purposes:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>2</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states,

<sup>2</sup>Recovery Act, § 5001.

and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>3</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs, (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs, and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, Georgia had drawn down \$311.5 million in increased FMAP grant awards, which is about 59.8 percent of its awards to date.<sup>4</sup> Officials noted that these funds were drawn down retroactively for the period October 1, 2008, through February 25, 2009, but funds can now be drawn down on a more frequent basis. Georgia officials reported they plan to use funds made available as a result of the increased FMAP to address increased caseloads, offset general fund deficits, and maintain current eligibility and benefit levels in the state Medicaid program.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Georgia provided these certifications, but qualified its maintenance of effort certification, noting that the Georgia General

<sup>3</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

<sup>4</sup>Georgia received increased FMAP grant awards of \$521.3 million for the first three quarters of federal fiscal year 2009.

## Appendix VII: Georgia

Assembly still was considering the Georgia Department of Transportation's (GDOT) fiscal year 2010 budget, which could impact the state's highway spending plans for that year.<sup>6</sup>

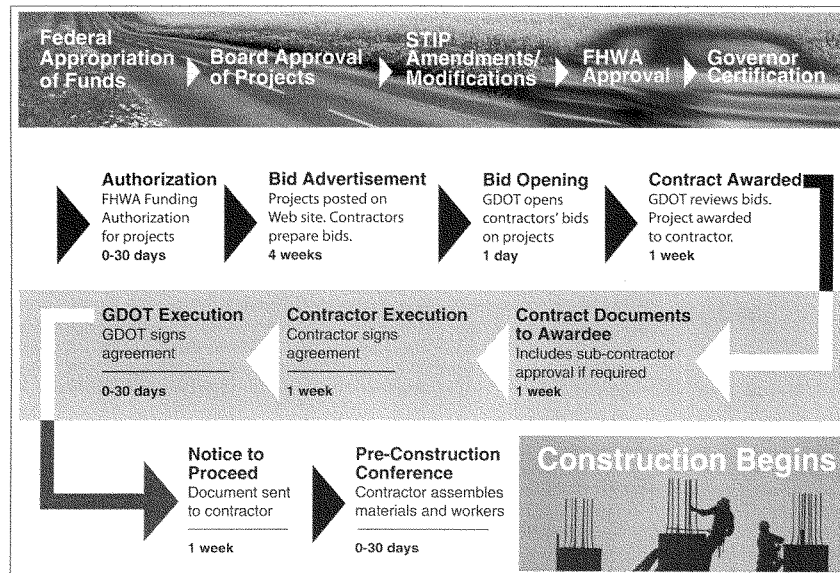
Georgia has been apportioned \$932 million for highway infrastructure. On April 7, 2009, the Governor certified the first round of projects to be funded with Recovery Act funds. As of April 16, 2009, the U.S. Department of Transportation had not obligated any Recovery Act funds for Georgia projects.<sup>6</sup> Georgia plans to spend \$208 million on 67 projects throughout the state. Of that amount, \$97 million will be spent in economically distressed areas. The funds will be spent on maintenance (53 percent), bridges (23 percent), capacity projects (17 percent), safety projects (6 percent), and enhancements (1 percent). The Georgia Department of Transportation plans to award contracts for the majority of these projects (73 percent) by May 22, 2009.<sup>7</sup> Figure 6 illustrates the implementation time line for Recovery Act highway projects.

<sup>6</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the Department of Transportation and has not been reviewed by GAO.

<sup>7</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

<sup>8</sup>The department will award most of the remaining contracts in June and July 2009.

Figure 6: Georgia Department of Transportation's Project Implementation Schedule



Source: Georgia Department of Transportation.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

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Georgia's initial SFSF allocation was about \$1 billion. According to state officials, the state's fiscal year 2010 budget passed on April 3, 2009, and included \$521 million in state fiscal stabilization funds for education and \$140 million in state fiscal stabilization funds for public safety.<sup>8</sup> Georgia plans to use the education funds for elementary, secondary, and public higher education. For instance, Georgia intends to use three established formulas to allocate funds to local education agencies, universities, and technical colleges. Georgia plans to use the public safety funds to help maintain safe staffing levels at state prisons, appropriately staff the state's forensic laboratory system, and avoid cuts in the number of state troopers. Georgia plans to submit its application for fiscal stabilization funds in late April or early May.

In addition to the major programs we discussed earlier, table 6 shows how Georgia and two local entities plan to use Recovery Act funds for other selected programs.<sup>9</sup>

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<sup>8</sup>The state's fiscal year runs from July 1 through June 30.

<sup>9</sup>The two local entities we visited were the Atlanta Housing Authority and the Atlanta Regional Workforce Board.

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Table 6: Planned Uses of Selected Recovery Act Funds

Selected programs	Anticipated funds (in millions of dollars)*	Examples of planned uses
<b>Transportation</b>		
Transit Capital Assistance Grants	144	Funds will be used to help with needs that were deferred as a result of budget cuts, such as bus replacement and the purchase of cleaner fuel vehicles.
Fixed-Guideway Infrastructure	7	Funds will go to the Metropolitan Atlanta Rapid Transit Authority.
<b>Education</b>		
Title I of the Elementary and Secondary Education Act of 1965 (commonly known as No Child Left Behind)	351 (grants to local education agencies); 104 (school improvement)	State will encourage local education agencies to focus on professional learning opportunities for staff and intervention programs for students who need help with math and writing.
Individuals With Disabilities Education Act, Parts B and C	339	Among other things, the state plans to encourage local education agencies to (1) provide professional development for special education teachers, (2) expand the availability and range of inclusive placement options for preschoolers, and (3) obtain state-of-the-art assistive technology devices and provide training in their use to enhance access to the general curriculum for students with disabilities.
<b>Other programs</b>		
Workforce Investment Act programs	88	State plans to use a portion for administration, oversight of local workforce agencies, as well as rapid response during major layoffs; the majority of the funds will be allocated to the 20 local areas within the state for adult, youth, and dislocated worker programs.  The Atlanta Regional Workforce Board—the local workforce board for seven counties in the Atlanta metropolitan area—is concentrating on plans for using the \$3.1 million it will receive for summer youth programs. <sup>†</sup>
Tax Credit Assistance Program	54	State will focus on fiscal year 2008 projects that received tax credits and those on the waiting list; for projects that received tax credits but are having difficulty using them, the state will either provide gap financing or exchange the tax credits for grants.
Public Housing Capital Fund	112 <sup>‡</sup>	The Atlanta Housing Authority will use \$18.6 million to rehabilitate 13 public housing developments and an additional \$8 million to complete the demolition of 3 public housing developments.
Neighborhood Stabilization Program	To be determined	State plans to apply, but the competition criteria have not yet been published.
Edward Byrne Memorial Justice Assistance Grants	36	State is currently developing a strategy to allocate the funds that must be passed through to local governments.

Source: GAO.

\*The anticipated funds are based on federal agency announcements as of April 17, 2009.

†The Atlanta Regional Workforce Board is administered by the Atlanta Regional Commission.

‡These funds go directly to local public housing authorities.

**In Addition to Addressing Specific Program Areas, Recovery Act Funding Also Will Help Mitigate Ongoing Fiscal Challenges**

The recent economic downturn adversely affected Georgia in a number of ways:

- Higher unemployment rate—as of February 2009, the state's unemployment rate was 9.3 percent. This rate surpassed the national unemployment rate (8.1 percent) and was almost double the state unemployment rate from a year earlier (5.4 percent).
- Increases in Medicaid enrollment—from January 2008 to January 2009, the state's Medicaid enrollment increased from 1,265,136 to 1,314,689, with increased enrollment attributable to three population groups: (1) children and families, (2) disabled individuals, and (3) other populations, which includes refugees and women with breast and/or cervical cancer.
- Declining revenue—through March 2009, the state's net revenue collections for fiscal year 2009 were 8 percent less than they were for the same time period in fiscal year 2008, representing a decrease of approximately \$1 billion in total taxes and other revenues collected.<sup>10</sup>
- Use of reserves—to offset shortages in revenue, the state used \$200 million from its Revenue Shortfall Reserve, or "rainy day" fund, in fiscal year 2009 and will use an additional \$259 million in fiscal year 2010.
- Recent budget cuts—overall, the state's budget was cut by 8 percent from fiscal year 2008 to fiscal year 2009.<sup>11</sup> As shown in table 2, some individual agencies were cut more significantly than others. Georgia officials plan to use Recovery Act funds to limit additional budget cuts.

<sup>10</sup>Net revenue collections for the month of March 2009 totaled \$988 million—compared with \$1.2 billion for March 2008, a decrease of 14.5 percent.

<sup>11</sup>This percentage represents the difference between the amended fiscal year 2008 budget and the amended fiscal year 2009 budget.



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Table 7: Budget for Selected State Agencies in Georgia, Fiscal Years 2008 and 2009

Selected state agencies	Amended fiscal year 2008 budget <sup>a</sup>	Amended fiscal year 2009 budget <sup>a</sup>	Percentage change from fiscal years 2008 to 2009
Department of Community Affairs	\$35,718,525	\$17,011,787	-52.4
Criminal Justice Coordinating Council	898,061	472,465	-47.4
State Accounting Office	7,205,916	4,089,053	-43.3
Department of Administrative Services	9,707,880	7,767,003 <sup>b</sup>	-20.0
Department of Community Health	2,347,794,015	1,879,185,744	-20.0
State Inspector General	833,534	679,410	-18.5
State Housing Finance Agency	3,287,829	2,700,020	-17.9
Department of Human Resources	1,631,068,194	1,394,208,017	-14.5
Department of Labor	55,081,172	47,934,616	-13.0
Office of Planning and Budget	9,474,735	8,419,050	-11.1
Department of Audits and Accounts	34,429,800	30,654,383	-11.0
Office of the Governor	7,653,328	7,113,270	-7.1
Department of Education	7,973,900,641	7,506,343,096	-5.9
Department of Transportation	832,725,819	865,193,794	3.9

Source: GAO analysis of Georgia Office of Planning and Budget data.

Notes: The state agencies in the table are those we interviewed or surveyed during this first reporting period. The Department of Administrative Services serves as the state's procurement office. The State Accounting Office serves as the state's controller. The Office of Planning and Budget is the state's budget office. The Department of Audits and Accounts is the state auditor.

<sup>a</sup>The amended budgets for fiscal years 2008 and 2009 represent state funds only.

<sup>b</sup>The fiscal year 2009 amount for the Department of Administrative Services includes \$5,424,149 in agency reserves used to supplement appropriations.

### Georgia Has Adapted Existing Processes to Approve Uses of Recovery Act Funding

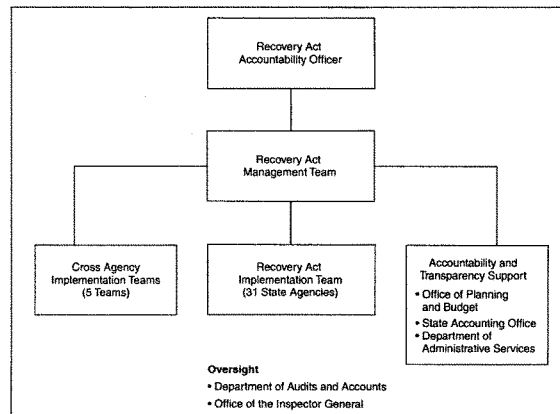
Georgia moved quickly to implement an infrastructure to manage Recovery Act funds. A small core team was in place as of December 2008 to begin planning for implementation. Within 1 day of enactment, the Governor had appointed a Recovery Act Accountability Officer, and she formed a Recovery Act implementation team shortly thereafter. The implementation team includes a senior management team, officials from 31 state agencies, a group to support accountability and transparency, and cross-agency teams (see fig. 7).<sup>15</sup> The Recovery Act Accountability Officer and senior management team are responsible for analyzing and

<sup>15</sup>The cross-agency teams work on initiatives such as energy, broadband, and competitive grants.

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disseminating federal and state guidance to the state agencies receiving Recovery Act funds. The accountability and transparency support group comprises representatives from the Office of Planning and Budget, State Accounting Office, and Department of Administrative Services. The State Auditor will serve as the primary auditor of the funds, and the Inspector General will provide investigative support and respond to complaints of fraud. The first implementation team meeting was held on February 24, 2009. Since then, the implementation team has met almost every week.

**Figure 7: Organizational Chart of Georgia's Recovery Act Implementation Team**



Source: Georgia Recovery Act Accountability Officer.

According to state officials, each year the Governor is required to present to the General Assembly a recommended state budget for the upcoming fiscal year and an amended budget for the current fiscal year. Prior to submitting the budget for the upcoming year, the Governor sets the state's revenue estimate, which when added to surplus and reserve funds, determines the size of the forthcoming appropriations bill. Furthermore, state officials told us that the Governor has the authority to approve the

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appropriations bill in its entirety or choose individual expenditure items to veto.<sup>13</sup>

To approve the use of Recovery Act funds, Georgia has enhanced its existing budget process. The majority of Recovery Act funds will be added into state budgets via an amendment process through the Governor's Office of Planning and Budget. A monthly Recovery Act budgeting and amendment process has been established to account for federal dollars. The Recovery Act approval process requires that each state agency submit an action plan to the Office of Planning and Budget that includes information on the agency, funding sources, accountability measures, and details on individual projects funded (see fig. 8).<sup>14</sup> For Recovery Act funds the state government receives, the budget office also is requiring state agencies to complete a tool that assesses risk. The budget office then reviews the plans submitted by the agency, provides feedback to the agency, and, in conjunction with the agency, finalizes the plans and risk assessment tool. The Governor, the Recovery Act Accountability Officer, budget office staff, and agency officials meet to vet the action plan and make a final decision on applying for funding. As of April 17, 2009, all state agencies had submitted action plans, and the budget office had begun its review of these plans.<sup>15</sup>

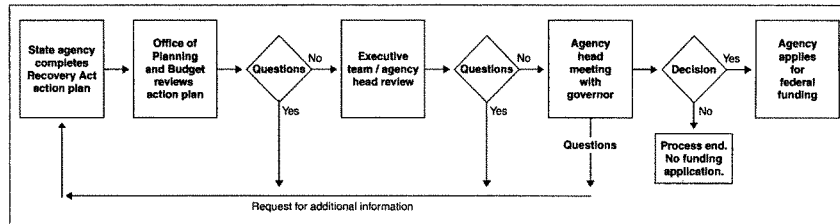
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<sup>13</sup>However, state officials noted that the legislature can override a gubernatorial veto with a two-thirds majority in each chamber.

<sup>14</sup>The actions plans were initially required to be submitted on February 12, 2009; however, due to delays in federal guidance, some state agencies were granted an extension until early March.

<sup>15</sup>The Department of Education was given an exemption, and weekly meetings were held with the Office of Planning and Budget to gather information in lieu of action plans.

Figure 8: State of Georgia Review Process for Recovery Act Funds



Source: Georgia Office of Planning and Budget.

Note: The executive team for the action plan process includes the Recovery Act Accountability Officer, the Chief Financial Officer, the Chief Operating Officer, the Governor's policy staff, Office of Planning and Budget staff, and agency officials.

## Georgia Has Been Establishing Internal Controls for Recovery Act Funds

Georgia's most recent Single Audit Act report identified a number of material weaknesses. Recognizing the risks associated with the influx of Recovery Act funds, the state has taken a number of steps to establish internal controls and safeguards for these funds.

### Georgia's Most Recent Single Audit Report Identified Material Weaknesses

Georgia's most recent Single Audit Act findings indicate that the state may have difficulty accounting for the use of some Recovery Act funds. In its fiscal year 2008 Single Audit report, the State Auditor identified 28 financial material weaknesses and 7 compliance material weaknesses. Three state agencies that expect to receive a substantial amount of Recovery Act funds were cited for most of the financial material weaknesses—the Department of Transportation (10), Department of Labor (4), and Department of Human Resources (2). For example, the Department of Transportation's financial accounting system was deemed unsuitable for day-to-day management. It also did not have a system in place to correctly identify fund sources, and as a result, auditors found that \$138 million of federal funds were misclassified.

In addition, auditors found that the Department of Labor was unable to provide detailed account balances for the Unemployment Insurance

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Program because it maintained an inadequate general ledger that consisted of manually updated spreadsheets.<sup>16</sup> The auditors also found that the Department of Human Resources' process of allocating indirect costs to programs had multiple deficiencies. They noted that inadequate internal controls and failure to follow established policies increases the risk of material misstatement in the financial statements, including misstatements due to fraud and noncompliance with federal regulation. In addition, the Department of Human Resources was cited for four compliance material weaknesses, such as requesting federal funds in excess of program expenditures.

To ensure that the affected state agencies will address these material weaknesses, the State Accounting Office will be monitoring corrective action plans developed in response to the Single Audit report. The office plans to issue guidance on the monitoring process by the end of April 2009 and has asked agencies to start tracking actions taken to address material weaknesses.

#### State Agencies Are Taking Steps to Safeguard and Oversee Recovery Act Funds

Georgia recognizes the importance of accounting for and monitoring Recovery Act funds and, despite recent budget cuts, has directed state agencies to safeguard Recovery Act funds and mitigate identified risks. At one of the first implementation team meetings, the Recovery Act Accountability Officer disseminated an implementation manual to agencies, which included multiple types of guidance on how to use and account for Recovery Act funds. For example, the Office of Planning and Budget provided details on the budgeting process for Recovery Act funds. New and updated guidance is disseminated at the weekly implementation team meetings. At the direction of the Recovery Act Accountability Officer, the three agencies tasked with accountability support—the Office of Planning and Budget, State Accounting Office, and Department of Administrative Services—and other state agencies have instituted the following safeguards:

- The Office of Planning and Budget, in collaboration with the State Accounting Office and others, is developing a state-level strategy to

<sup>16</sup>The state expects to receive about \$236 million in Recovery Act funds for unemployment insurance (\$220 million for unemployment insurance benefits and \$16 million for administration).

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monitor high-risk agencies.<sup>17</sup> Additional risk-mitigation strategies will be developed and implemented for these agencies.

- The State Accounting Office issued two accounting directives to all state agencies. The first provides guidance on accounting for Recovery Act funds separately from other funds. The state plans to use Catalog of Federal Domestic Assistance numbers to track Recovery Act funds separately. Funds will also be segregated through a set of unique Recovery Act fund sources in the state's financial accounting system. For example, the state is tracking increased FMAP funds for Medicaid through the development of a unique identifier for each grant award. The second accounting directive supplies language that should be included in all contracts issued under the Recovery Act. In addition, the office is reviewing the current accounting internal controls and assessing how they can be enhanced for Recovery Act funds.<sup>18</sup>
- The Georgia Department of Administrative Services plans to issue a communication alert stating that any state agency planning to award contracts with Recovery Act funds should contact the department for guidance. The department has developed standard contract language that should be included in all Recovery Act contracts and plans to publicize and offer training for state agency contracting staff. Further, the department plans to continue its compliance reviews of agencies with delegated purchasing authority to ensure they are following proper policies and procedures.<sup>19</sup>
- All of the agencies we met with that directly administer programs had monitoring processes in place that they plan to adapt or enhance for Recovery Act oversight. For example, the Georgia Department of Community Affairs' plans for monitoring the Tax Credit Assistance

<sup>17</sup>Certain state agencies have been identified as high risk due to their size, the potential for reorganization, and outdated financial reporting systems.

<sup>18</sup>The majority of state agencies use PeopleSoft, the state's current financial reporting system, to track their expenditures. However, there are some agencies that do not use this system and others that have greatly customized the software for their agency's individual use.

<sup>19</sup>A state official reported that the Georgia Department of Community Health is developing a separate contracting and vendor management process for any contracts that are needed or awarded to carry out the functions of grants that may be awarded to vendors as a result of the Recovery Act. Existing performance outcomes will be applied to the new contracting mechanism and are expected to provide early indicators regarding the need to apply additional audits or controls.

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Program include a front-end analysis of costs, third-party inspections prior to the release of funds, and an audit of the general contractor by a certified public accountant. The last requirement is unique to projects funded with Recovery Act tax credits.

In addition, the State Auditor, Inspector General, and internal audit divisions within state agencies have taken or plan to take the following steps to mitigate risk and oversee the use of Recovery Act funds:

- The State Auditor issued two audit risk alerts. One urged all agency officials to include appropriate contractual provisions in Recovery Act contracts and to not rush the distribution of Recovery Act funds before adhering to proper internal control processes and understanding federal guidelines. The other alert discussed limits on the use of funds. The State Auditor also plans to provide internal control training to state agency personnel in late April. The training will discuss basic internal controls, designing and implementing internal controls for Recovery Act programs, best practices in contract monitoring, and reporting on Recovery Act funds.
- Currently, the State Auditor conducts routine statewide risk assessments as a means of identifying high-risk agencies and determining where to best focus audit resources.<sup>20</sup> Officials plan to target future risk assessments on programs receiving Recovery Act funding and are awaiting additional audit guidance from the Office of Management and Budget (OMB).
- The Inspector General issued a directive requiring all state agencies to insert new contractual language in any contracts, subcontracts, grants, and bid solicitations financed with Recovery Act funds.<sup>21</sup> The new language specifically gives her the right to inspect all records of outside vendors, subcontractors, and consultants.
- In conjunction with the State Accounting Office, the Inspector General plans to conduct unannounced visits to state agencies receiving Recovery Act funding.

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<sup>20</sup>The risk assessments evaluate a program's previous audit findings, internal controls, and material weaknesses based on pre-established criteria.

<sup>21</sup>The Inspector General is part of the executive branch.

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- The Inspector General also developed a database to specifically track Recovery Act complaints and a public service announcement to alert the public of how to report fraud, waste, and abuse.
- Some state agencies, such as the Departments of Human Resources and Transportation, have internal audit divisions that plan to monitor the use of Recovery Act funds. For instance, the Department of Human Resources' internal auditor has developed a plan to assess the risk of each program prior to receiving Recovery Act funding.

#### Resources Available for Oversight May Be Limited

As these actions and plans indicate, Georgia recognizes the importance of instituting safeguards for Recovery Act funds. However, state officials also stressed the costs of such efforts. Both the Governor's Office and the State Auditor noted that they had not received additional funding for Recovery Act oversight. As shown in table 2, several agencies with oversight responsibilities experienced significant budget reductions in fiscal year 2009, including the State Accounting Office (43 percent), Inspector General (19 percent), Office of Planning and Budget (11 percent), and State Auditor (11 percent).

The State Auditor noted that, if state fiscal conditions do not improve or federal funding does not become available for audit purposes, additional budget and staffing cuts may occur within the department. Directives from OMB, due by May 1, will provide guidance on the audit requirements for Recovery Act programs. Officials noted that the scope of pending audit requirements may greatly impact the State Auditor's ability to audit Recovery Act programs on top of existing audit requirements. In addition, some state officials that directly administer programs told us that overseeing the influx of funds could be a challenge, given the state's current budget constraints and hiring freeze. In some cases, state agencies told us that they planned to use Recovery Act funds to cover their administrative costs. Other state agencies wanted additional clarity on when they could use program funds to cover such costs.

#### Plans to Assess Impact of Recovery Act Funds Are in Initial Stages

In general, Georgia is awaiting additional federal guidance on reporting requirements before making detailed plans to assess impact. However, the State Auditor is adapting an existing system (used to fulfill its Single Audit Act responsibilities) to help the state report on Recovery Act funds. The statewide Web-based system will be used to track expenditures, project status, and job creation and retention. The state will make data from this system available on its Recovery Web site. The Governor is requiring all state agencies and programs receiving Recovery Act funds to use this



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system. State officials do not expect to track and report on funds going directly to localities, but some said they would like to be informed of these funds so that the state can coordinate with localities. They cited broadband initiatives and health funding to nonprofit hospitals as areas where a lack of coordination could result in a duplication of services or missed opportunities to leverage resources.

In addition, some state agencies appear to have more experience tracking jobs than others. For example, the Georgia Department of Community Affairs has experience tracking jobs for the Community Development Block Grant program; therefore, agency officials do not expect to have difficulty tracking jobs for the Neighborhood Stabilization Program. For another program it will administer, the Tax Credit Assistance Program, Community Affairs surveyed potential applicants in March 2009 to gain a better understanding of performance measures that could be tracked as a part of its monitoring efforts, including job creation. In contrast, officials from other programs, such as the Edward Byrne Memorial Justice Assistance Grant program and the Transit Capital Assistance Grant program expressed concerns about identifying appropriate measures of job creation and retention within the purpose of their programs and were waiting for more guidance from federal agencies and OMB.

### Georgia's Comments on This Summary

We provided the Governor of Georgia with a draft of this appendix on April 17, 2009. The Recovery Act Accountability Officer responded for the Governor on April 19, 2009. In general, she noted that the report accurately and succinctly captures the implementation status of the Recovery Act process in Georgia.

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### Staff Acknowledgments

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## Appendix VIII: Illinois

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, highways, and the State Fiscal Stabilization Fund.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$892 million in increased FMAP grant awards to Illinois.
  - As of April 1, 2009, Illinois has drawn down about \$117.1 million, or about 12 percent of its initial increased FMAP grant awards.
  - Illinois plans to use funds made available as a result of the increased FMAP in fiscal years 2009 and 2010 to fill a Medicaid budget gap, permitting the state to move from an average 90-day payment cycle to a cycle of no more than 30 days for all of its providers, including payments hospitals and nursing homes.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Illinois was apportioned about \$936 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated \$606.3 million for 214 Illinois projects. Illinois Department of Transportation officials stated that they will award most contracts based on a competitive bidding process, but they will use a quality based selection process for approximately \$27 million in engineering services contracts.
  - These projects include activities such as resurfacing highways and repairing bridge decks.
  - Illinois will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Illinois was allocated about \$1.4 billion from the initial release of these funds on April 2, 2009 by the U.S. Department of Education. On April 20, 2009, these funds became available to the state. Illinois is expecting to receive an additional \$678 million by September 30, 2009.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. The state submitted its application on April 10, 2009.
  - Illinois plans to use all of its \$2 billion in State Fiscal Stabilization funds for K-12 and higher education activities to address the layoffs and other cutbacks many district and public colleges and universities are facing in their fiscal year 2009 and 2010 budgets.

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Illinois is also receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA); and two programs of the U.S. Department of Agriculture—one for administration of the Temporary Food Assistance Program and one for competitive equipment grants targeted to low income districts from the National School Lunch Program.

**Safeguarding and transparency:** To provide accountability and transparency in how these funds are being spent, the state has established a high level Executive Committee and a separate working group to oversee Recovery Act compliance across agencies and departments. It has also developed a Web site ([www.recovery.illinois.gov](http://www.recovery.illinois.gov)) that contains information about the use of Recovery Act funds. The state is in the process of performing a risk assessment of all state programs receiving Recovery Act funds to identify potential vulnerabilities. It will use the state's Single Audit—a state-level audit of the largest programs receiving federal money—as a tool in identifying these risks. State agencies also reported that they are capable of tracking their Recovery Act funds separately from other program funds by tagging them with a special accounting or funding code. For the most part, these codes will permit agencies to then rely on existing processes to monitor and report on how these funds are being spent.

**Assessing the effects of spending:** Officials at several state agencies indicated that they can track various performance measures for projects funded through the Recovery Act by utilizing existing systems. However, according to officials in the Governor's office and other state agencies, more guidance is needed on definitions for job creation and retention measures to adequately measure their impact.

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## Illinois Beginning to Use Recovery Act Funds

Illinois has started to use some of its Recovery Act funds, and high level state officials we spoke with described several overarching priorities and goals that the state plans to achieve through use of these funds. These include averting layoffs and creating new jobs, concentrating resources on economically distressed areas, and funding infrastructure improvements, as described below.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons

with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

From January 2008 to January 2009, Illinois's Medicaid enrollment increased slightly from 2,184,963 to 2,298,802, with the highest share of the enrollment increase attributable to two population groups: (1) children and families and (2) non-disabled non-elderly adults. Illinois is estimated to receive a total of \$2.9 billion in increased FMAP funding, of which \$992 million has already been awarded to the state for the first three quarters of federal fiscal year 2009. For the second quarter of federal fiscal year 2009, Illinois received an FMAP of 60.48 percent—an increase of 10.48 percentage points over its fiscal year 2008 FMAP. As of April 1, 2009, Illinois has drawn down \$117.1 million in Recovery Act funds, which is almost 12 percent of the amount awarded to Illinois to date. Illinois state officials indicated that the main focus in using funds made available as a

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

result of the Recovery Act will be to meet financial obligations and to ensure compliance with the prompt payment provisions of the Recovery Act.<sup>3</sup> Specifically, Illinois is using funds made available as a result of the Recovery Act to fill a Medicaid budget gap, permitting the state to move from a 90-day payment cycle to a 30-day cycle for all of its providers, including payments to hospitals and nursing homes. The state has also decided to include pharmacists in its prompt payment initiative. These actions will also help avoid potential layoffs in provider organizations.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending. The governor or other appropriate chief executive must also certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Illinois provided the first of these certifications but noted that the state's level of funding was based on the best information available at the time of the state's certification.<sup>4</sup>

The Illinois Department of Transportation (IDOT) is planning to spend a large share of its estimated \$655 million in Recovery Act funds<sup>5</sup> for highway and bridge construction and maintenance projects in

<sup>3</sup>Under the Recovery Act, to be eligible for the increased FMAP, states must comply with prompt payment requirements, which require states to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt.

<sup>4</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>5</sup>According to the Federal Highway Administration, Illinois' share of Recovery Act funds for highway infrastructure investment is approximately \$936 million. This total consists of \$655 million for IDOT projects and \$281 million in suballocations for local government highway projects. The \$655 million to IDOT includes \$627 million for IDOT to use statewide and \$28 million for mandatory transportation enhancements. Transportation enhancements include activities such as provision of facilities for pedestrians and bicyclists, preservation of abandoned railway corridors, acquisition of scenic easements, and historic preservation projects.

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economically distressed areas. Equally important criteria are that projects must be shovel-ready and can be completed by February 2012. These funds will expand the amount of money the state can invest in highway projects beyond the amounts the state had listed in its State Transportation Improvement Program. The projects will include resurfacing roads across the state, repairing bridge decks, replacing guardrail sections, and improving pavement markings. As of April 16, 2009, the U.S. Department of Transportation had obligated \$606.3 million for 214 Illinois projects.<sup>8</sup> IDOT officials stated that they will award most contracts based on a competitive bidding process, but they will use a quality based selection process for approximately \$27 million in engineering services contracts.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers. The Illinois Office of the Governor submitted the state's application for these funds to Education on April 10, 2009. On April 20, 2009, these funds became available to the state. Illinois is expecting to receive an additional \$678 million by September 30, 2009.

The U.S. Department of Education has allocated a total of about \$2 billion in SFSF monies to Illinois. Approximately \$1.4 billion of this amount was allocated in an initial release on April 2, 2009. Illinois plans to use all of the \$2 billion from the SFSF for K-12 and higher education activities and hopes to avert layoffs and other cutbacks many districts and public colleges and universities are facing in their fiscal year 2009 and 2010 budgets. State Board of Education officials also noted that U.S. Department of Education guidance allows school districts to use stabilization funds for education reforms, such as prolonging school days

<sup>8</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed. Illinois will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.

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and school years, where possible. However, officials said that Illinois districts will focus these funds on filling budget gaps rather than implementing projects that will require long-term resource commitments.

**Additional Plans for Use of Funds Made Available as a Result of the Recovery Act Include Offsetting State's Budget Deficit and Implementing New Capital Plan**

The State of Illinois has been in a recession since December 2007 and continues to face financial difficulties. The state's unemployment rate surged by 46 percent from 5.9 percent in February 2008 to 8.6 percent in February 2009. Major job losses are expected to continue in manufacturing, construction, and retail. On the housing front, foreclosure filings in February 2009 were up 62 percent over 2008. While state general fund revenue grew 4.5 and 5.7 percent in fiscal years 2007 and 2008, respectively, revenues declined by 0.5 percent in fiscal year 2009. The state estimates that it faces a projected \$11.6 billion operating budget deficit for fiscal years 2009 and 2010. To address this deficit, the Governor has proposed a number of measures in the state's 2010 budget proposal, including the following:

- Spending cuts, including 4 furlough days for state employees and a 2-percent spending reduction in grant programs;<sup>7</sup>
- State employee pension reform, including provisions that would align the state's eligible age for full benefits with that of Social Security, adjust benefit formulas, and increase contribution rates for current employees;
- Creation of a taxpayer board to improve accountability and efficiency across state programs; and
- Revenue increases, including income tax increases that would raise an estimated \$2.8 billion from individuals and \$350 million from corporations in fiscal year 2010; higher health care contributions from current and retired state employees; and higher vehicle registration, title, and license fees.

Illinois officials expect that the state will receive at least \$9 billion in direct Recovery Act funds to the state, and those local entities—such as public housing and transit authorities—will receive additional Recovery

<sup>7</sup>According to the proposed Illinois fiscal year 2010 budget, the 2 percent reductions in grant programs will exclude healthcare and education programs.

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Act funds. State officials said they have identified about \$4.3 billion of Recovery Act funds, including use of the previously mentioned SFSF, that could be utilized to address the operating budget shortfall for fiscal years 2009 and 2010.<sup>8</sup> They noted that these funds would potentially reduce pressure on the state for further tax increases and spending cuts. In addition, the state plans to use some of the remaining Recovery Act funds to help launch the Governor's proposed infrastructure building program—a \$26.5 billion proposal to fund schools, roads and bridges, public transit, and energy and environmental capital projects during Illinois fiscal years 2010 through 2015. The \$26.5 billion plan would be paid for with funds from the state (\$10.6 billion), federal sources (\$11.6 billion), local sources (\$2.4 billion), and the Recovery Act (\$2.0 billion).<sup>9</sup>

In addition to funds administered by state agencies, local entities will also receive funds through the Recovery Act for programs administered at the local level. We met with one local agency that will receive Recovery Act funds and will use its funds to address overdue capital improvements. The Chicago Transit Authority (CTA), an independent governmental agency that provides rail and bus service in the greater Chicago area, has already put plans in place to spend its \$240 million. CTA has a backlog of \$6.8 billion in unfunded capital projects necessary to update its infrastructure and fleet. The agency has begun work on an \$87.8 million project that will replace rails, ties, and fasteners for one subway line. The agency also expects to complete hybrid bus purchases, a bus and rail car fleet overhaul, and numerous facility improvements by the end of 2009. Finally, reconstruction of at least one rail station is expected to be completed by late 2010.

While we found examples of programs that have received Recovery Act funds and have projects that are already underway, we spoke with state officials who said they needed more guidance about how they should use, track, and report on these funds at their agencies. State Board of Education officials said that understanding the reporting requirements and

<sup>8</sup>State officials told us Governor Pat Quinn recently signed a supplemental appropriations bill to give the state spending authority for Recovery Act funds during the remainder of fiscal year 2009. To allow for the use of Recovery Act funds in fiscal year 2010, the General Assembly must approve the fiscal year 2010 budget bill. The presentation of the fiscal year 2010 budget did not occur until March 18, 2009, due to the impeachment and removal of the prior Governor in January 2009. State officials were not certain as to when the General Assembly will pass the fiscal year 2010 budget.

<sup>9</sup>Individual amounts do not sum to \$26.5 billion due to rounding.



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eligible uses for Recovery Act funds is the biggest challenge they face as they prepare to disseminate funds to the local school districts. They also expressed concern with the Recovery Act's dual emphases on accountability and quick expenditure of funds. The Illinois Criminal Justice Information Authority expressed similar concerns about the need for federal guidance in regard to reporting time frames that may not completely align with previous reporting procedures.

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### Illinois Is Taking Steps to Assess Risk and Develop Plans for Safeguards Related to Recovery Act Funds

During our meetings with high-level state officials, they said that efforts are underway to ensure accountability and transparency in the use of Recovery Act funds. The Governor's office has established an Executive Committee and working group to identify concerns across state agencies and help them implement Recovery Act provisions. Also, state internal audit officials are developing a variety of internal control techniques to assure compliance with the Recovery Act's requirements. To properly track funds, state agency officials explained that they plan to use unique identifiers or codes so that these funds can be separately tracked in their existing financial or grants management systems.

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### Illinois Has Established a Recovery Act Executive Committee and Working Group

To ensure accountability and transparency in the use of Recovery Act funds, the state has established an Executive Committee, a Recovery Act Working Group, and an Illinois Recovery Web site. The Executive Committee is comprised of state executives, including the Deputy Chief of Staff for Economic Recovery, the Chief Internal Auditor, the Budget Director, and the Chief Information Officer. According to state officials we spoke with, the Executive Committee is working to identify common risks to all state agencies in the use of Recovery Act funds. To address crosscutting Recovery Act issues, such as legal matters and procurement, the committee is also establishing subcommittees with agency subject matter experts to review critical information and develop policies on these subject matters.<sup>10</sup> The Recovery Act Working Group consists of a contact point for each state agency for Recovery Act related matters and, according to state officials, meets to communicate requirements, guidance, and implementation related to the act.

The Governor's Office has also established an Illinois Recovery Web site at [www.recovery.illinois.gov](http://www.recovery.illinois.gov), which contains information on the programs

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<sup>10</sup>At the time of our meetings, these subcommittees were still being formed.

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receiving Recovery Act funds, amounts available through the act, and certifications signed by the Governor.<sup>11</sup> The Web site will also include reports on Recovery Act program expenditures, and eventually users will have the ability to download raw data on project or program descriptions, budgets, spending, and job creation. Another feature of Illinois's Web site is that it allows the public to submit suggestions for projects that the state could fund through the Recovery Act.

#### State Audit Officials Are Developing Internal Control Measures

Every state is required to have an annual Single Audit in accordance with U.S. Office of Management and Budget (OMB) requirements. This audit is required when \$500,000 or more in federal funds is expended in any fiscal year. Officials from the Illinois Office of Internal Audit (OIA) stated that they will utilize the Office of the Auditor General's (OAG) single audits to identify programs that may require additional scrutiny. In Illinois's fiscal year 2007 Single Audit, the OAG identified four material weaknesses in internal controls over financial reporting and classified 46 findings as significant deficiencies and material weaknesses in internal controls related to compliance. Significant agency findings classified as a material weakness that are relevant to the Recovery Act and recipients of Recovery Act funds included

- The State Board of Education not sanctioning a Local Education Agency that did not meet the comparability of services requirement under the Title I Grants to Local Educational Agencies Program;
- IDOT not obtaining certifications from subrecipients for not having been suspended or debarred from participation for the Airport Improvement Program;
- Multiple agencies inadequately conducting or failing to conduct on-site monitoring of subrecipient awards for federal programs; and
- Multiple agencies inadequately monitoring subrecipient audit reports for federal programs.

<sup>11</sup>To receive certain Recovery Act funds, among other requirements, the state's governor must certify that: (1) the state will request and use funds provided by the act; and, (2) the funds will be used to create jobs and promote economic growth. Recovery Act, div. A, title XVI, § 1607.

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The OAG explained that to the extent that federal programs receiving Recovery Act funds are addressed in the OMB compliance supplement, it will be performing its required audit procedures. The OAG stated that OMB guidance will be critical for planning future audits of federal funds. Furthermore, the OAG conducted an analysis of programs receiving Recovery Act funds, and found that a few additional programs will likely be included in future single audits. OIA officials told us that they are using the Single Audit results to assist in conducting a risk assessment of all state-administered programs receiving Recovery Act funds. OIA officials said that they will use the results of this risk assessment to target their audit efforts to programs that demonstrate a high level of risk. OIA and OAG officials said that they plan to follow up on their respective prior audit findings to make sure that state agencies have taken appropriate corrective action. OIA officials said that in addition to large programs, they plan to follow up on prior internal audit findings on federal Recovery Act programs under \$30 million that are not covered by the statewide single audit.

**State Agencies Plan to Use Unique Identifiers or Codes to Track Recovery Act Funds**

Most agency officials we spoke with stated that their systems are capable of tracking Recovery Act funds separately from other funds for the same programs. For example, IDOT officials stated that Recovery Act projects are being noted in different systems, typically with special funding codes. In addition, when IDOT officials access Recovery Act funds, those transactions will have special codes and notations. Similarly, officials at the Illinois Department of Human Services told us that any funds the agency receives through the Recovery Act for the Neighborhood Stabilization Program will have accounting codes separate from any previous funds received through the program. In order to track increased FMAP funds, Illinois officials said they will use the state's existing accounting systems and will use existing processes to review and reconcile expenditures. For example, state officials will record draw downs of increased FMAP funds separately from other Medicaid funds. State officials will also use special receipt, expenditure, and contract codes for all increased FMAP funds and related Medicaid expenditures. A CTA official we spoke with stated that his agency will use its existing financial system to track Recovery Act funds by unique project numbers or descriptions. Finally, officials from the State Comptroller's Office told us that separate appropriation codes will likely be used to track Recovery Act expenditures statewide. One agency official indicated that while funds can easily be tagged at the state level, he was concerned that this might not be the case once funds are distributed to subrecipients.

### Agencies Are Considering Ways to Assess Impacts, but Additional Guidance Is Needed

Officials at several state agencies we spoke with indicated that they can use various performance measures for projects funded through the Recovery Act by utilizing existing systems. For example, IDOT officials stated that they will track and monitor data for Recovery Act projects in the same manner as they do for regular program reporting, and should be able to report on and provide evidence regarding the status of project goals and objectives. Officials with the Illinois Housing Development Authority stated that they also track performance and goals for each project through current systems and should be able to build on these systems to customize reports as necessary for the Recovery Act.

On the other hand, several state officials said that additional guidance is needed for measuring the potential impact of Recovery Act funds. According to officials from the Governor's office and state agencies we spoke with, additional guidance is needed on definitions of "jobs saved," "jobs created," "jobs sustained," and other similar terms included in the Recovery Act. Illinois Department of Commerce and Economic Opportunity officials stated that they had concerns regarding the evaluation of job retention as it relates to the Workforce Investment Act program. Specifically, they said OMB Recovery Act guidance focuses on quick job placement, but jobs created through the act may have lower retention than those under past program grants. Furthermore, while officials at most agencies we visited stated that they are considering plans to track the impact of Recovery Act funds, none of these plans have been finalized. Officials at two state agencies said that their systems do not track such specific performance measures, and they may need to develop additional mechanisms to link Recovery Act funds with their performance results.

### Illinois's Comments on This Summary

We provided the Governor of Illinois with a draft of this appendix on April 17, 2009. The Deputy Chief Of Staff responded for the Governor on April 20, 2009. In general, the state concurred with our statements and observations. The official also provided technical suggestions that were incorporated, as appropriate.

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**Staff  
Acknowledgments**

In addition to the contacts named above, Paul Schmidt, Assistant Director; Tarek Mahmassani, Analyst-in-Charge; Rick Calhoon; Katherine Iritani; David Lehrer; Lisa Reynolds; and Mark Ryan made major contributions to this report.

## Appendix IX: Iowa

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation, and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage Funds**
  - As of April 3, 2009, Centers for Medicare and Medicaid Services (CMS) had made about \$84 million in increased FMAP grant awards to Iowa.
  - From January 2008 to January 2009, Iowa's Medicaid enrollment increased from 358,112 to 392,813, with the highest enrollment increase attributable to two population groups: (1) children and families and (2) nondisabled nonelderly individuals.
  - As of April 15, 2009, Iowa had drawn down about \$86 million, or 63 percent of its increased FMAP grant awards.
  - Officials plan to use funds made available as a result of the increased FMAP to cover increased caseloads, maintain existing populations of recipients, and avoid reductions to benefits for Medicaid recipients.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Iowa was apportioned about \$358 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated \$221.2 million for 107 Iowa projects.
  - As of April 15, 2009, the Iowa Department of Transportation had competitively awarded 25 contracts valued at \$168 million, or 47 percent of the Recovery Act funds apportioned.
  - Contracts were awarded for projects such as bridge replacements and highway resurfacing—"shovel ready" projects that could be initiated and completed quickly.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Iowa was allocated about \$316 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments.
  - Iowa plans to submit its application as soon as it can be accurately completed.
  - Iowa's Department of Education plans to use these funds to maintain spending for grades K-12 and postsecondary education at fiscal year 2009 levels for fiscal years 2010 and 2011.

In addition, Iowa estimates that other funding will be provided to the state under the Recovery Act for the following program areas:

- Education—\$214 million (includes programs such as those to provide grants to local education agencies and assist individuals with disabilities).
- Housing and infrastructure—\$252 million (includes programs such as the Weatherization Assistance Program).
- Agriculture/natural resources—\$152 million (includes programs such as the clean water state revolving fund).
- Economic development—\$94 million (includes programs such as the unemployment insurance program).

The status of plans for using these funds is discussed throughout this appendix.

**Safeguarding and transparency:** Iowa has a foundation of safeguards and controls that could help assure proper spending of Recovery Act funds. For example, the State Auditor is responsible for audits of state and local entities, such as counties, cities, and school districts, and must provide guidelines to public accounting firms that perform such audits. In addition, many state agencies have internal audit groups that focus on programmatic and financial issues. Furthermore, according to state officials, administrative and statutory mechanisms are in place that could oversee Recovery Act funds and provide information to the public on how these funds are being spent. For example, while previous audits have shown few financial weaknesses, the State Auditor is updating its 2009 audit plan risk assessment to reflect the increased risk associated with Recovery Act funding. Iowa is also enhancing its accounting systems to track all Recovery Act funds that will flow through the state government to ensure that the state can adjust its spending plans as needed. Furthermore, Iowa is developing or planning systems to track funds provided to cities, counties, local governments, and other entities. Finally, Iowa is working to establish a framework that will provide transparency on the use of Recovery Act funds. This framework includes the state's Recovery Act Web site, which is designed to provide up-to-date information on the use of Recovery Act funds by program, a state board to recommend improvements to existing practices to prevent fraud, waste, and abuse and oversee the spending of Recovery Act funds, and mechanisms provided through the state's Accountable Government Act.

**Assessing the effects of spending:** State agencies have begun to consider how to measure outcomes and assess the effect of the Recovery Act. Some agencies have mechanisms in place to collect data in order to calculate outcomes. Other state agencies are awaiting guidance such as a consistent approach to quantifying the number of jobs created and sustained. In the meantime, Iowa's Legislative Services Agency plans to work closely with the Iowa Department of Management to create outcome measures for the Recovery Act and report results.

## Iowa Beginning to Use Recovery Act Funds

Most Iowa state officials said they plan to follow established allocation formulas while waiting for federal guidance on the use and tracking of Recovery Act funds. For example, the Iowa Department of Economic Development, which manages the state's Community Development Block Grants and Neighborhood Stabilization Program, intends to follow the state-established allocation formula for the Community Development Block Grants program. This formula allocates funding in thirds: one-third to affordable housing, one-third to economic development, and one-third to infrastructure.

Some agencies have gone even further in their spending of Recovery Act funds. For example, the Iowa Department of Transportation has funded some "shovel ready" projects within 3 days of the enactment of the Recovery Act. Additionally, the Iowa Department of Economic Development has already established guidance for allocating Neighborhood Stabilization Program funding to eligible entities, should the state be awarded competitive grant funds.

As of April 15, 2009, Iowa had drawn down about \$86 million of its increased FMAP grant awards for the Medicaid program, which is 63 percent of its awards to date. The state plans to use funds made available as a result of the increased FMAP to cover increased caseloads and maintain current levels of benefits, noting that without these funds, the program would have faced budget shortfalls. Additionally, the state plans to use \$110 million of funds made available as a result of the increased FMAP to fully fund Medicaid in the current fiscal year and \$145 million of these funds to fully fund Medicaid in fiscal year 2010.

Iowa has begun to use some of its Recovery Act funds, as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons



with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, CMS made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

For the first two quarters of 2009, Iowa's FMAP rate was 68.82 percent, a 7.09 percentage point increase over fiscal year 2008. Iowa has received increased FMAP grant awards of \$136 million for fiscal year 2009, and, as of April 15, 2009, Iowa had drawn down \$86 million in increased FMAP grant awards, which is about 63 percent of its awards to date. Iowa officials indicated they will use funds made available as a result of the increased FMAP to cover increased caseloads, maintain existing populations of recipients, avoid cuts to eligibility, and maintain current levels of benefits. In addition, such funds will provide Iowa officials with the means to offset budget shortfalls, including shortfalls for the state's Medicaid program. Iowa officials indicated that they expect the recession to continue longer for the state than for the nation as a whole, and if the increased FMAP funds are not available for all of federal fiscal year 2011,

<sup>1</sup>Recovery Act div. B, title V § 5001.

<sup>2</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

the resulting deficit will likely be addressed through the use of reserve funds or cuts in program funding. According to state officials, the use of FMAP funds requires an appropriation from the state legislature.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for existing programs, and in addition, the Governor must certify that the state will maintain its current level of transportation spending, and the Governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Iowa's Governor certified that the state would "maintain its efforts" for Department of Transportation programs funded under the Recovery Act. However, Iowa noted in its certification that transportation spending would be influenced by the difference in the definition of the word "expend" for different covered programs; the uncertainty of the amount collected from state user fees to fund the programs; and variables (such as weather) that may affect the state's timeline for spending Recovery Act transportation funds.<sup>3</sup>

Within 3 days of the enactment of the Recovery Act, the Iowa Department of Transportation competitively awarded contracts for 19 highway and bridge projects valued at about \$56 million. Contracts were awarded for projects such as bridge replacements and highway resurfacing—shovel-ready projects that could be initiated and completed quickly. As of April 15, 2009, Iowa had competitively awarded a total of 25 contracts valued at \$168 million, or 47 percent of the Recovery Act funds apportioned. As of April 16, 2009, the U.S. Department of Transportation had obligated \$221.2 million for 107 Iowa projects.<sup>4</sup> According to Iowa transportation officials,

<sup>3</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>4</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

the agency could begin spending Recovery Act funds quickly because it maintained an inventory of shovel-ready projects and its accounting system needed few changes to track the projects.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF), to be administered by the U.S. Department of Education. The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to the U.S. Department of Education that assures, among other things, that it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

On April 2, Iowa was allocated \$316 million for the education portion of the SFSF. Overall, Iowa expects that the state's total SFSF allocation will be \$472 million. In April, the Governor proposed using almost 82 percent of this amount, or \$386 million, to support elementary, secondary, and higher education, as required. These funds will be used for activities such as updating standards and implementing a new data system. For the remaining 18 percent of the SFSF allocation, or \$86 million, the Governor proposes to fund universities and community colleges, law enforcement, and corrections in fiscal year 2010. The Governor also proposed using \$600,000 of the \$86 million to oversee Recovery Act funds. Iowa plans to submit its application as soon as the application can be accurately completed.

#### Iowa Has Established a Strategy for Spending Recovery Act Funds

Beginning in April 2008, unemployment began to rise and in October 2008, state revenues began to slow. As of February 2009, Iowa's unemployment rate was 4.9 percent, up from 3.9 percent in February 2008. According to a March 27, 2009, report by the Rural Policy Research Institute, the nation's rural economy is losing jobs at a rate faster than the rest of the United States. Iowa state budget officials estimated that the state's unemployment rate could increase to 7 percent by December 2009.

Regardless of this economic downturn, Iowa's Governor and General Assembly have statutory responsibility to balance the budget and meet expenditure limitations and are required to use the revenue estimates agreed to by Iowa's Revenue Estimating Conference, which convenes quarterly, as the basis for determining the budget for the general fund, according to state officials. If revenue estimates are revised downward for the current fiscal year, state officials explained that the law still requires

the budget to be balanced. In the current fiscal year, and for the first time since fiscal year 2003, Iowa's general fund revenues of almost \$6 billion are expected to be lower than in the previous fiscal year, a decrease of 1.9 percent from fiscal year 2008 to fiscal year 2009.<sup>5</sup> In response to this downturn, in December 2008, the Governor directed an across-the-board 1.5 percent reduction in the state's general fund appropriations, effective December 22, 2008. On April 3, 2009, the Governor released a revised budget for fiscal year 2010 of \$5.9 billion for the state's general fund, representing a 7.9 percent reduction for many state programs, even with the addition of more than \$535 million in Recovery Act funds. According to state officials, decisions regarding the use of Recovery Act funds require approval by the General Assembly. Since the Iowa General Assembly is scheduled to adjourn on or around May 1, 2009, it may have to develop strategies if funding decisions are necessary after adjournment. For example, the Governor may request that the General Assembly return for a special session.

In March 2009, the Governor established a Recovery Act implementation working group to provide a coordinated process for (1) reporting on Recovery Act funds available to Iowa through various federal grants and (2) tracking the federal requirements and deadlines associated with those grants. The implementation working group comprises representatives from nearly two dozen state agencies, led by an executive-level working group, and assisted by groups that will focus on implementation issues such as budget and tracking, intergovernmental coordination, and communications. The implementation working group includes several issue-specific small groups focusing on key program areas: education, energy, environment, health care, housing, information technology, public safety, transportation and infrastructure, and workforce. On April 14, 2009, the working group issued a progress report on Recovery Act funds in Iowa. For example, the working group reported on the planned and spent funding of the state's energy program to reduce per capita energy consumption, loans for wastewater infrastructure projects, and neighborhood stabilization programs to provide emergency assistance to acquire and redevelop foreclosed properties.

<sup>5</sup>Iowa's fiscal year begins July 1 and ends June 30.

In addition to FMAP, Transportation, and the State Fiscal Stabilization Fund programs, the Governor's office estimates that the state will receive Recovery Act funding as follows:

- Education: Of \$214 million, a large majority involves two formula grant programs—grants to local education agencies (\$52 million) and special education grants to assist individuals with disabilities (\$122 million).
- Housing and infrastructure: Of \$252 million, 32 percent (\$81 million) is for the Weatherization Assistance Program to provide energy-related improvements to homes and educate residents about energy conservation.
- Agriculture/natural resources: Of \$152 million, more than one-third (36 percent or \$54 million) is for the clean water state revolving fund.
- Economic development: Of \$94 million, more than three-quarters (76 percent or \$71 million) is to modernize the unemployment insurance program.

To supplement Recovery Act funds, Iowa is considering other stimulus proposals, such as the Iowa Infrastructure Investment Initiative, or I-JOBS, and another bonding initiative. I-JOBS is designed to create jobs, strengthen the state's economy, and rebuild the state's infrastructure over 3 years. If approved by the General Assembly, I-JOBS, as described by state officials, is expected to provide funding for various infrastructure projects, such as transportation, public buildings, and wastewater improvements, and will be funded through 20-year tax-exempt bonds paid for by gaming revenue, current tax revenue, or both. The General Assembly is also considering another bonding initiative to provide economic stimulus. As of April 17, 2009, the Iowa General Assembly had not authorized the issuance of bonds for either of these initiatives.

In the absence of OMB and program-specific guidance, associations and organizations have provided guidance and assistance to Iowa on the use and reporting of Recovery Act funds. Among these associations are the National Association of Crime Victim Compensation Boards, the National Association of Victims of Crime Act Assistance Administrators, and the Association for Stop Violence Against Women Administrators. For example, justice associations have helped the Iowa Attorney General's Office complete grant applications.

### Iowa Is Developing Systems to Track Recovery Act Funds

Many Iowa agencies expect that they will be able to track the Recovery Act funds they use through the state's central accounting system. The state is also evaluating options for reporting Recovery Act funds provided to cities, counties, local governments, and other entities that will help satisfy reporting requirements for these funds. Specifically, state accounting officials are developing special codes to track Recovery Act funds and have begun to train state agencies' accounting officials in the use of these new codes. However, Iowa's central accounting system does not track Recovery Act funds provided directly to some agencies because they are not part of the system. For example, the central accounting system does not track Recovery Act funding provided to the Iowa Department of Transportation. In this case, Iowa transportation officials said the agency is establishing separate accounting codes to track Recovery Act funds by project. Similarly, the central accounting system does not track Recovery Act funds provided to state-funded universities. The state and Board of Regents are discussing how to track these funds. While local governing authorities are not required to report through the state, the Iowa Department of Management is in discussions with these entities to report Recovery Act spending on the state's Web site. At the local level, some agencies can track these funds, while others are developing guidance to require such tracking, according to state officials.

In order to track increased FMAP funds, Iowa is adapting its existing systems. In addition, Iowa's state Medicaid agency uses a data warehouse for Medicaid payments made to counties, subcontractors, and medical facilities, and U.S. Health and Human Services' Office of Inspector General has audited the state's data warehouse.

The General Assembly may also track Recovery Act spending. In particular, the assembly's Legislative Services Agency—a nonpartisan analysis and research agency serving the Iowa General Assembly—assisted members in interpreting the Recovery Act and provided preliminary estimates of funds provided to the state. Furthermore, the Legislative Services Agency will be able to access Iowa's central accounting system to monitor agencies' spending in real time.

Even as Iowa plans for tracking Recovery Act funds, state officials said that they continue to have some questions about how to report Recovery Act funds. For example, Iowa officials noted that they need additional guidance on reporting increased FMAP funds to CMS. Specifically, Iowa officials said that they need guidance on the timing for drawing down increased FMAP grant awards, reporting receipts and expenditures, and submitting claims for expenditures made retroactively to October 2008.

**Iowa Has a Foundation of Safeguards and Controls That Could Help Assure Proper Spending of Recovery Act Funds**

There are various entities in Iowa that are responsible for monitoring, tracking, and overseeing financial expenditures, including the Iowa State Accounting Enterprise (collects and reports state financial information and processes financial transactions); the State Auditor (audits state and local entities, such as counties, cities, and school districts, and provides guidelines to public accounting firms that perform such audits); and the Attorney General (prevents and prosecutes fraud). Finally, many state agencies have internal audit groups that focus on programmatic and financial issues.

**While Prior Audits Indicate Few Financial Weaknesses, State Auditor Is Identifying Potential Areas Needing Oversight**

Prior years' audits indicate few weaknesses in Iowa's financial management systems and controls. Iowa's fiscal year 2007 single audit found one material weakness in internal controls related to a public assistance grant provided to the Iowa Department of Transportation: a computer program error resulted in a \$3.6 million overpayment to the agency by the Federal Emergency Management Agency for materials related to disaster recovery. In 2009, Iowa refunded the \$3.6 million. Iowa's fiscal year 2008 single audit did not identify any material weaknesses.

While prior audits indicate few financial weaknesses, the Office of the State Auditor is updating its 2009 audit plan risk assessment to reflect the increased risk associated with Recovery Act funding. Of great concern to officials of the State Auditor's office are possible limits on the ability to charge fees for audit services. According to state officials, these limits would significantly reduce the effectiveness of the State Auditor to audit federal funds received, including those under the Recovery Act, as required by the Single Audit Act. If limits on audit fees were enacted, officials said that the state's comprehensive annual financial report and the single audit report are likely to result in qualified opinions.

**Iowa Has Administrative and Statutory Mechanisms in Place That Could Help Oversee Iowa's Recovery Act Funds**

The Iowa state government is working to establish a framework to provide transparency on the use of Recovery Act funds. In March 2009, the Governor's office launched an economic Recovery Act Web site—[recovery.iowa.gov](http://recovery.iowa.gov)—to provide information on Recovery Act funding by program. Iowa plans to add a "dashboard" feature to the Web site—a user-friendly search capability that will provide detailed information on how and where Recovery Act funds are spent. The Governor's office expects OMB to provide guidance on how to report information on Iowa's Recovery Act Web site, including the dashboard feature, and how to

forward that information to the national Recovery Act Web site. In addition, the state is developing a system that will allow information on Recovery Act funding that does not come through the state government, such as grants federal agencies provide directly to localities, to be available on the state's Web site.

On April 14, the Governor created the Iowa Accountability and Transparency Board—which has similarities to the federal Recovery Accountability and Transparency Board—to, among other duties, assess existing practices to prevent fraud, waste, and abuse; recommend opportunities for improvement in these areas; and oversee real-time audits and reporting. The board will be made up of 14 members. Voting members include the Governor or his designee, the State Auditor or his designee, the State Treasurer or his designee, three local government members, and three citizens. Nonvoting members of the board include the Director of Iowa's Department of Management or his designee and four members of the state's General Assembly. The Iowa Accountability and Transparency Board will recommend improvements and oversee the spending of Recovery Act funds.

Iowa's Accountable Government Act could serve as a mechanism to safeguard Recovery Act funding. Under this act, Iowa is required to provide for the efficient and effective use of state funds. Among other things, Iowa's Accountable Government Act requires grant recipients to certify that information on internal controls relating to processes are available for inspection by the state agency, and the Legislative Services Agency if the recipients provide a service of more than \$500,000 that is paid for with local, state, or federal funds. In addition, recipients must report on financial information, reportable conditions in internal control or material noncompliance, and corrective actions taken or planned in response to these reportable conditions. State agencies can enforce this monitoring by terminating payments and recovering any expended government funds. Furthermore, the Legislative Services Agency tracks personnel services contracts—that is, contracts for consulting services or temporary hires—within all state agencies (except the Iowa Department of Transportation and the Iowa Board of Regents) regardless of the value of the contract. State officials could require a similar certification and monitoring of Recovery Act funds.

Iowa officials said that they recognize the need for greater oversight and proper management of programs in light of the infusion of significant funds under the Recovery Act. According to state officials, the Recovery Act did not provide funds for oversight. For example, one state agency



official in the Iowa Department of Education expressed concern about the adequacy of resources available for ensuring the appropriate use of the Recovery Act funds—an estimated \$386 million from the state fiscal stabilization program for education—particularly because the agency anticipates further state-imposed staff reductions. Recognizing that the Recovery Act did not specifically provide funds for state oversight, the Governor proposed using \$600,000 of the \$86 million in fiscal stabilization funds in his 2010 budget to be made available for general government services to oversee Recovery Act funds.

Iowa officials indicated that they are identifying ways to use the state's internal audit functions to address Recovery Act-related issues. Iowa state audit officials indicated that state programs that receive significant Recovery Act funds while maintaining a high level of discretion over use of those funds—such as the state's Medicaid program—present an increased risk to the state and will receive greater scrutiny during internal state audits.

### State Agencies Are Considering How to Assess the Effects of Recovery Act Funds

Iowa has just begun to consider how to measure outcomes and assess the effect of Recovery Act funding while it awaits federal guidance on a consistent approach to measuring the number of jobs created and sustained. State officials identified Iowa's Accountable Government Act as a mechanism that has familiarized state agencies with results-oriented management and could help them assess the impact of Recovery Act funds. The Iowa Accountable Government Act requires each state agency to measure and monitor progress toward achieving program goals and report the progress toward those goals. In addition, the Iowa Department of Management, in consultation with the Legislative Services Agency, the State Auditor, and agencies, must periodically conduct performance reviews to assess the effectiveness of programs and make recommendations to improve agency performance.

State agency officials said that they expect to be able to track information on the number of jobs created while others said they need further guidance. For example, the Iowa Department of Transportation tracks the number of worker hours by highway project on the basis of contractor reports. An Iowa Transportation official said that this information may be used to calculate the number of jobs created. Iowa education officials, in contrast, may need more guidance. Iowa teachers are notified by school districts in mid-March whether their jobs are guaranteed for the next school year, pending passage of school budgets. Once the budgets are passed, teachers are asked to return for the following school year.

## Appendix IX: Iowa

Officials said that they believed that federal guidance would help them determine how to characterize whether these jobs would be created or sustained.

According to Iowa's Department of Management, once it receives federal guidance on how to assess the impact of Recovery Act funding, it plans to disseminate the information across state agencies. It intends to measure the impact of Recovery Act funds through the state's Recovery Act Web site and current tracking software. The Legislative Services Agency plans to work closely with the Department of Management to create outcome measures for the Recovery Act and report the results. Additionally, the Iowa Department of Economic Development has already established output and outcome measures for the Neighborhood Stabilization Program.

Although most state agencies are waiting for federal guidance on how to assess results from Recovery Act funding, officials from some state agencies told us that they have accounting systems in place to measure programmatic outcomes. For example, the Iowa Department of Economic Development will monitor its Recovery Act funds by using systems adopted for tracking federal disaster recovery funds, including systems that the federal Department of Housing and Urban Development uses to monitor and report on funding spent to recover from natural disasters. The Iowa Department of Economic Development plans to put in place procedures for working with the State Auditor to leverage oversight of stimulus funds. Similar procedures have been established to oversee funding the state expects to receive to recover from disastrous floods in 2008. The Department of Economic Development expects a 20-fold increase in Community Development Block Grants in 2009 to help the recovery effort from these floods.

Officials noted the potential difficulty of measuring Recovery Act outcomes separately from other recovery initiatives, such as Iowa's proposed I-JOBS program. While state officials said that they believe there are benefits to supplementing federal efforts, the state may find it difficult to separate outcomes among the recovery programs.

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**Appendix IX: Iowa**

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**Iowa's Comments on  
This Summary**

We provided the Governor of Iowa with a draft of this appendix on April 17, 2009. The Director, Iowa Office of State-Federal Relations and the Director for Performance Results, Department of Management responded for the Governor on April 20, 2009. In general, officials agreed with our findings and conclusions. The officials also offered several technical suggestions that we have incorporated, as appropriate.

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**Staff  
Acknowledgments**

In addition to the individuals named above, Thomas Cook, Assistant Director; Christine Frye, Analyst-in-Charge; Alisa Beyninson; Gary Brown; Daniel Egan; Nancy Glover; Marietta Mayfield; Mark Ryan; and Carol Hermstadt Shulman made key contributions to this appendix.

## Appendix X: Massachusetts

### Overview

**Use of funds:** An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation, and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage Funds**
  - As of April 1, 2009, Centers for Medicare & Medicaid Services (CMS) had made about \$1.2 billion in increased FMAP grant awards to Massachusetts.
  - As of April 1, 2009, the state had drawn down about \$273 million, or 23 percent, of its initial increased FMAP grant awards.
  - Officials plan to use funds made available as a result of the increased FMAP to avoid additional cuts in health care and social service programs, restore certain provider rates, and provide caseload mitigation for Medicaid and Commonwealth Care (an expansion of its Medicaid program).
- ✓ **Transportation—Highway Infrastructure Investment**
  - Massachusetts was apportioned about \$425 million for highway infrastructure investment as of April 16, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated about \$63.9 million for 19 projects in Massachusetts.
  - As of April 4, 2009, the Massachusetts Executive Office of Transportation had advertised 19 projects for competitive bids totaling more than \$62 million; the earliest announcements were scheduled to close on April 14, 2009, and work on the projects is expected to begin this spring.
  - These projects include activities such as road repaving and sign replacement.
  - Massachusetts will request reimbursement from the U.S. Department of Transportation as project phases are completed by contractors.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Massachusetts was allocated about \$666 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. In early April 2009, state officials reported that the commonwealth will file its application for this money around April 15, 2009, when it would better understand the state fiscal year 2010 budget situation.
  - The Governor has announced that he intends to provide funds to 166 school districts to help them increase spending to prior levels and avoid program cuts and teacher layoffs in fiscal year 2010. He also intends to use some of these funds at public colleges and universities to reduce layoffs, program cuts, and student fee hikes.

## Appendix X: Massachusetts

The commonwealth of Massachusetts is also receiving additional Recovery Act funds under programs, such as Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA, commonly known as No Child Left Behind); the Individuals with Disabilities Education Act, Part B (IDEA); and two programs of the U.S. Department of Agriculture—one for administration of the Temporary Food Assistance Program and one for competitive equipment grants targeted to low-income districts from the National School Lunch Program. The status of plans for using Recovery Act funds is discussed throughout this appendix.

**Safeguarding and transparency:** Task forces, established by the Governor, encouraged the state to adopt accountability and transparency measures. Further, Massachusetts is expanding its accounting system to track funds flowing through the state government. Although Massachusetts has plans to publicly report its Recovery Act spending, officials have said that the state may not be aware of all funds sent directly to other entities, such as municipalities and independent authorities. The commonwealth's oversight community has identified situations that raise concerns about the adequacy of safeguards, such as funding for larger projects and new programs, but is waiting for further information on what specific programs will receive funding before developing plans to address those concerns.

**Assessing the effects of spending:** Massachusetts agencies are in the early stages of developing plans to assess the effects of Recovery Act spending. According to state officials, they are awaiting further guidance from the federal government, particularly related to measuring job creation.

## Massachusetts Beginning to Use Recovery Funds

Massachusetts has begun to use some of its Recovery Act funds, as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal

matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act are for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

Under the Recovery Act, the commonwealth's FMAP will increase to at least 56.2 percent, up from 50 percent. As of April 1, 2009, Massachusetts had drawn down \$272.6 million, or 23 percent, of its increased FMAP grant awards. In fiscal years 2009 and 2010, officials plan to use a significant portion of funds made available as a result of the increased FMAP funds to avoid additional cuts in health care and social service programs, restore certain provider rates, and provide caseload mitigation for Medicaid and Commonwealth Care.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways, and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary

<sup>1</sup>Recovery Act, §5001.

<sup>2</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

legal reviews and determined that the projects are an appropriate use of taxpayer funds. Massachusetts provided these certifications, but conditioned the state's level of funding for these programs, noting that this spending will be financed through issuing bonds and may need to be decreased, depending on the state of the economy. The commonwealth's debt affordability policy will determine the amount of debt that can be issued.<sup>3</sup>

As of April 4, 2009, the Massachusetts Executive Office of Transportation had advertised 19 projects for competitive bid totaling more than \$62 million. These projects included, for example, replacing traffic and guide signs along sections of Route I-95 and paving Route 6 in southeastern Massachusetts. As of April 16, 2009, the U.S. Department of Transportation had obligated about \$63.9 million for 19 projects in Massachusetts.<sup>4</sup> Massachusetts will request reimbursement from the U.S. Department of Transportation as project phases are completed by contractors.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF is intended to help states avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Massachusetts' initial SFSF allocation is \$666,152,997. In early April 2009, state officials reported that the state would file its application for this money around April 15, 2009, when it would better understand the state's revenue projections and after the Massachusetts House issues its fiscal year 2010 budget proposal. In March 2009, the Governor of Massachusetts had announced he intended to fund \$168 million in SFSF to 166 school

<sup>3</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>4</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

districts to help them increase funding and avoid program cuts and teacher layoffs in fiscal year 2010. He also announced he intended to provide \$162 million in SFSF to public university and college campus budgets to reduce layoffs, program cuts, and student fee hikes.

#### Massachusetts' Planning Process Has Set the Stage for Decisions on Spending of Recovery Act Funds

Massachusetts officials began preparing for receipt of federal Recovery Act funds prior to enactment of the act. Faced with deteriorating revenue projections, the potential for expanding caseloads in some safety net programs, such as Medicaid, and a requirement to balance the budget, Massachusetts officials believe that funds made available as a result of the Recovery Act are critical to addressing the commonwealth's immediate fiscal pressures. State officials envision a sizable portion of the state-projected \$8.7 billion in Recovery Act funds (over 2 years) going directly toward budget stabilization. According to state officials, as of April 2009, the state is addressing a budget gap of approximately \$3.0 billion. This gap is driven largely by lower-than-anticipated revenues. State fiscal year 2009 revenue is significantly lower than budgeted and has left the state unable to support previously approved spending levels, and revenues are expected to fall short of planned expenditures for 2010, as well.

In December 2008, anticipating a major infusion of federal funding, especially for infrastructure projects, the Governor established task forces to identify "shovel-ready" projects and address obstacles to project implementation. Ten task forces were created—seven focused on specific types of infrastructure investment, such as transportation, energy, and information technology, and three focused on crosscutting issues like workforce mobilization and procurement. In conducting their work, the task forces were guided by several principles, including investing for the long term and limiting investments to those that would not add to the state's operating budget.

Although other program areas, such as Medicaid and education, likely will receive more funding than will infrastructure, the work of the task forces was influential. The task forces developed work plans for projects that could be implemented using the anticipated funding and were instrumental in the appointment of a director of infrastructure investment (a "recovery czar") to coordinate and monitor state agencies' and municipalities' implementation of projects. The task forces also encouraged the creation of a central Web site to enhance transparency, called for the involvement of the oversight community in contract oversight to ensure accountability, and prompted the introduction of legislation (now being considered by the legislature) intended to ease



some of the procurement and contracting processes that might delay quick implementation of construction projects. The task force efforts helped prepare the state to submit several certifications required under the Recovery Act to the federal government. In late February, the Governor certified that the state would request and use all funds provided by the act. Additional certifications for transportation and energy have also been submitted.

Revenue from the state's "rainy-day" fund,<sup>5</sup> a reserve fund built up during more favorable economic conditions to be used during difficult economic times, will give the commonwealth additional flexibility to avoid some cuts in fiscal year 2010. The commonwealth's budget already calls for using about \$925 million from the rainy-day fund in fiscal year 2009, and the Governor's proposed 2010 budget calls for using about \$489 million of the rainy-day funds. According to budget documents, the combination of funds made available as a result of the increased FMAP and rainy-day funds will help the state avoid cuts in several areas, including health care, education, and public safety.

State documents suggest that officials are concerned about using one-time federal and rainy-day funds to make longer-term operational and program commitments that could require additional revenue in the future to avoid job and service cuts.<sup>6</sup> State officials note that using temporary funds, such as Recovery Act and rainy-day funds, make budgeting uncertain and require strategic fiscal management.

<sup>5</sup>Massachusetts officials refer to rainy-day funds as stabilization funds. However, to avoid confusion with the Recovery Act's State Fiscal Stabilization Fund, we will use rainy-day funds.

<sup>6</sup>The Governor's budget proposal for fiscal year 2010 includes several revenue enhancement proposals, including increased meals and hotel taxes and eliminating a sales tax exemption on alcohol, candy, and sweetened beverages.

## Appendix X: Massachusetts

**Massachusetts Has a System to Track Recovery Act Funds but Cannot Ensure Local Entities' Ability to Meet Recovery Act Reporting Requirements**

The commonwealth is expanding the use of its existing accounting system to track all Recovery Act funds that will flow through the state government. New codes are being added to the existing system in order to segregate and track the Recovery Act funds. The Office of the Comptroller has issued guidance on the required use of these newly created account codes for all Recovery Act transactions and has stipulated that all the Recovery Act-funded contracts include provisions to segregate Recovery Act money. While these changes have been made, officials were still testing the system and developing reporting capabilities as of April 13, 2009.

The portion of Recovery Act funds going directly to recipients other than Massachusetts government agencies, such as independent state authorities, local governments, or other entities, will not be tracked through the state comptroller's office. While state officials acknowledged that the commonwealth lacks authority to ensure adequate tracking of these funds, they are concerned about the ability of smaller entities to manage Recovery Act funds—particularly municipalities that traditionally do not receive federal funds and that are not familiar with Massachusetts' tracking and procurement procedures, as well as recipients receiving significant increases in federal funds. In order to address this weakness, the administration introduced emergency legislation that, according to state officials, includes a provision requiring all entities within Massachusetts that receive Recovery Act money to provide information to the state on their use of Recovery Act funds. Alternatively, the two large nonstate government entities we spoke with to date—the city of Boston and the Massachusetts Bay Transportation Authority (MBTA, a quasi-independent authority responsible for metropolitan Boston's transit system)—believe that their current systems, with some modifications, will allow them to meet Recovery Act requirements. For example, the city of Boston hosted the Democratic National Convention in 2004, and city officials said that their system was then capable of segregating and tracking a sudden influx of one-time funds.

**State Agencies Have Made Some Spending Decisions**

Some state programs have received actual allocations of federal Recovery Act funds, while for other state programs, officials have developed spending plans based on preliminary figures provided by federal departments. The U.S. Department of Transportation, through the Federal Transit Administration, published apportionment amounts for the Transit

Capital Assistance and the Fixed Guidance Infrastructure Investment Programs on March 5, 2009.<sup>7</sup> The Massachusetts Executive Office of Transportation (EOT) and the MBTA have been able to develop spending plans with a degree of certainty and EOT has advertised requests for bids on 19 projects totaling about \$62 million. Other program officials have had to develop plans with preliminary estimates. For example, as of mid-March 2009, state officials from the Department of Elementary and Secondary Education said that local education officials reported that one of their biggest challenges was a lack of reliable information on federal Recovery Act allocations that they could use to plan their budgets. However, on April 1, 2009, Education announced the release of state allocations of ESEA Title I and IDEA funds, along with more detailed guidance for these programs.

Some state and local officials said that while clear, specific guidance takes time to develop, the lack of guidance from federal agencies had limited their ability to make spending decisions. Officials from some of the entities we spoke with, including the state Department of Elementary and Secondary Education, the Department of Housing and Community Development, and the city of Boston, said they are comfortable making spending decisions with money slated to flow through pre-existing grant programs. However, the lack of specific guidance for federal Recovery Act funds for some programs has presented challenges, according to some state officials. An area of significant challenge for education officials concerns how to use federal Recovery Act funding to supplement state and local revenues for existing educational programs, rather than use these funds to supplant state and local revenue. State education officials said they anticipated that to prove funds have not been supplanted will be very challenging for local school districts and have requested additional guidance from the U.S. Department of Education to help them make better decisions about spending priorities. For example, state housing officials are seeking clarification from the U.S. Department of Housing and Urban Development (HUD) on whether the Tax Credit Assistance Program can be used to provide loans rather than grants to subrecipients, and state transportation officials are waiting for guidance on whether competitive grants can be used for "signature projects."

Some state agencies told us they anticipate they will be able to manage additional Recovery Act funding coming through well-established grant

<sup>7</sup>Federal Register / Vol. 74, No. 42 / Thursday, March 5, 2009 / Notices.

programs with existing agency resources but, in some cases, will hire additional staff to manage Recovery Act programs. For example, the state's Department of Housing and Community Development (DHCD) reported it is expecting to receive significant Recovery Act funds and has plans to hire staff to help manage the programs. DHCD has well-established methods for managing expenditures and accomplishments, so agency officials believe they can effectively administer Recovery Act funds using existing structures. MBTA officials told us that given the enhanced transparency and reporting requirements associated with an additional \$230 million in project spending, they anticipate that managing these Recovery Act projects will present some new challenges and will require that they hire a project management firm. Finally, a Department of Elementary and Secondary Education official told us they anticipate a need to hire additional staff, for a limited term, to manage competitive grant programs funded under the Recovery Act.

### Plans for Safeguards and Controls Being Developed at State Level

The commonwealth has entities responsible for monitoring, tracking, and overseeing financial expenditures. The comptroller, who is responsible for implementing accounting policies and practices, oversees fiscal management functions, including internal controls. The State Auditor audits the administration and expenditure of state funds, and partners with an accounting firm to perform the state's annual Single Audit—a comprehensive review of all state agencies' accounts and activities. The state Inspector General, with a broad mandate to prevent fraud, waste, and abuse, conducts operational and management reviews and has authority to examine independent authorities and municipalities. The Attorney General also plays a role, including preventing and prosecuting fraud. Further, according to state officials, some state departments have internal audit groups that focus on programmatic issues. In addition to these entities, the commonwealth has laws that provide further safeguards.

### Potential Areas of Vulnerability with Massachusetts Recovery Act Funds

Past experience has shown financial management vulnerability involving organizations that will receive funds under the Recovery Act. The Office of the Attorney General has documented improper Medicaid payments and has concerns regarding the funds from the Recovery Act going to the Medicaid program. They plan to take a risk-based approach, but are waiting for firm information on which programs and recipients will receive Recovery Act funds. The Inspector General stated that his office will need to emphasize oversight of larger procurement projects, which may be vulnerable. In addition, officials pointed to the multibillion-dollar cost overruns on a federally funded highway project in Boston (the "Big Dig")

as an example of what can go wrong when a large project lacks sufficient oversight. The Massachusetts fiscal year 2007 Single Audit report identified vulnerabilities that included insufficient monitoring of subrecipients of federal grants to the state. For example, the Massachusetts Department of Early Education and Care programs, which will receive Recovery Act funds, did not conduct any on-site monitoring of the Child Care Resource and Referral Agencies (subrecipients), which received approximately \$11 million in child care development funds and \$122 million in Temporary Assistance for Needy Families funds. Since that audit, the department has implemented numerous improvements and controls to address these issues. The State Auditor has also identified financial management concerns with nonprofit entities that receive federal funds and will receive additional funds under the Recovery Act.

In addition, oversight officials noted some more general situations raising concerns. For example, some oversight officials identified new programs as potentially risky; however, new programs would have little impact on the fiscal year 2009 Single Audit report. New programs would probably be included on the fiscal year 2010 Single Audit report, which typically comes out some months after the end of the state's fiscal year. Oversight officials also expressed concern about programs receiving large increases under the Recovery Act, and recipients that do not typically receive federal funds—and therefore may not have systems in place to track them—are also at risk.

In order to better understand areas of potential vulnerability, the Governor asked all commonwealth agencies in late January 2009 to conduct self-assessments identifying existing oversight and accountability mechanisms. Most agencies submitted reports, which included varying levels of detail. The reports we reviewed showed that the agencies are generally comfortable with the mechanisms currently in place. One report expressed a need for additional resources to oversee any new funding. The self-assessments were shared with the State Auditor, Inspector General, and Comptroller's offices. The State Auditor has provided comments to the Governor's office, noting that while the self-assessments indicated existing control mechanisms in place to manage, account for, and monitor the spending of the Recovery Act funds, he expressed two areas of concern. He was concerned about tracking funds that bypass the state government and, based on past audits, about subgrantee monitoring. The Inspector General plans to provide comments on the needs assessments to the Governor's office by the end of April. The Comptroller is using the assessments to monitor agencies' controls over Recovery Act funds on an ongoing basis.

### Plans for Oversight of Massachusetts' Recovery Act Funds

While the commonwealth's oversight community has come together to discuss issues such as avoiding areas of duplication and preventing oversight gaps, as a whole, it has yet to develop a coordinated plan describing which programs and departments it will focus on or how it will conduct critically needed oversight. Both the Inspector General and Attorney General recognize the need for training for local officials, specifically related to procurement. The Inspector General stated that his department would continue its training of local procurement officials and announced in its March 2009 Procurement Bulletin that his office should be contacted regarding any questions on procurement or Recovery Act expenditures. While the Inspector General identified the need for increased oversight, particularly related to procurements, oversight officials generally stated that once they determine the total distribution of Recovery Act money, they then would begin selecting areas for review. The Attorney General has convened a task force to coordinate on oversight issues with the federal and state oversight community.

The state legislature will also provide oversight of the Recovery Act funds through the newly created Joint Committee on Federal Stimulus Oversight. This committee has already held three hearings with plans to hold more regarding the oversight of Recovery Act spending. According to committee members, the impetus for creating this committee was Massachusetts' failure to control fraud, waste, and abuse in the federally funded "Big Dig" construction project. The purpose of the joint committee is to ensure compliance with federal regulations and to review current state laws, regulations, and policies to ensure they allow the commonwealth to access Recovery Act funding and streamline processes to quickly stimulate the economy. In addition to the co-chairmen having the capability to subpoena individuals, a co-chairman said that the Joint Committee has broad authority and its jurisdiction extends to wherever public federal, state, and local money is spent.<sup>8</sup>

Massachusetts' administration has emphasized transparency of Recovery Act spending and identified the state recovery Web site as a transparency tool. In addition, the Web site has links to planning documents, guidance, and intended uses of Recovery Act money, and officials are planning to enhance the Web site with a goal of making it the central portal for all

<sup>8</sup>The Joint Committee's jurisdiction covers wherever federal, state, and local money is spent within the commonwealth with the exception of the spending by the Massachusetts legislature.

## Appendix X: Massachusetts

Recovery Act information and reporting. Their goal is to include the ability to track Recovery Act money by town and by project, as well as to include each project's budget, schedule, awarded contracts (with contract details), and its on-time status. In addition, the public can send e-mails regarding stimulus issues to this site and the Recovery czar's staff is responsible for replying.

**Availability of Resources for Oversight**

Several Massachusetts officials expressed concern that the Recovery Act did not provide funding specifically for state oversight activities, despite the importance of ensuring that Recovery Act funds are used appropriately and effectively. In addition, the task forces the Governor convened in December 2008 concluded that it is critical the Inspector General and State Auditor have resources to audit Recovery Act contracts and management of Recovery Act funds, as well as recommended that the Attorney General's office should be provided with the resources to promptly and effectively pursue fraud and abuse.

However, due to the present economic conditions, state officials said the Massachusetts oversight community is facing budget cuts of about 10 percent at a time when increased oversight and accountability is critically needed. To illustrate the impact of the impending budget situation, the Inspector General told us that his department does not have the resources to conduct any additional oversight related to Recovery Act funds. This significantly impacts the Inspector General's capacity to conduct oversight since the budget of the Inspector General's office is almost entirely composed of salaries, and any cuts in funding would result in fewer staff available to conduct oversight. In addition, the State Auditor described how his office has already furloughed staff for 6 days and anticipates further layoffs before the end of fiscal year 2009. Similar to the Inspector General's office, 94 percent of his department's budget is for labor and any cuts in funding generally result in cuts in staff.

Some of these vulnerabilities may be mitigated by emergency legislation that the Governor recently filed, which included a provision to allow the pooling of administrative costs. This new legislation may make some Recovery Act funds available to the audit community for oversight, as long as federal law permits. Meanwhile, officials stated they are moving forward with developing and implementing enhancements to the Massachusetts recovery Web site, yet they are doing so without any Recovery Act funds. One senior state official stated she did not believe the Recovery Act provided funding for any state-level centralized information technology planning or development but noted that the Recovery Act

provided a considerable level of funding for information technology development at the program level.

### Plans to Assess Impact of Recovery Act Funds Are in Initial Stages

Although they are awaiting federal guidance on how to assess the impact of the Recovery Act, Massachusetts agencies are in the process of considering how to assess the number of jobs that will be created. For example, officials from DHCD are examining different methodologies for identifying job creation, while the city of Boston is using an economic forecasting model to evaluate job creation and other economic effects of projects. In addition, DHCD officials told us that they asked Tax Credit Assistance Program project managers to report estimates on the number of jobs, by trade, that will be needed to complete projects and are also looking for a reliable economic forecasting model to use for this reporting objective. DHCD officials also said they are waiting for guidance from HUD on how to calculate and document job creation for programs funded under the Neighborhood Stabilization Program. DHCD officials said they plan to use a pre-existing process developed for community action programs to collect information on job creation for projects funded by the Weatherization Program. MBTA officials said they feel confident they can estimate the number of new jobs created using Recovery Act funds; however, they are waiting for specific guidance from the U.S. Federal Transit Administration or the Office of Management and Budget on what to include in job creation calculations, as well as how to track indirect (jobs created to manufacture goods used in the project) and leveraged jobs (jobs created by new building projects that result from transportation improvements). MBTA officials also said they are looking to outsource some of the required oversight, including documenting job creation. Finally, state transportation officials are concerned that incentives may encourage contractors to overinflate the number of jobs created by their projects. They told us that, in the absence of specific guidance on how to account for job creation, some smaller contractors might overreport the number of jobs created. Furthermore, the cold weather conditions in the commonwealth can prohibit construction from continuing during the winter months. Officials suggested the pressure to show that the projects are contributing to the recovery may encourage some contractors to inflate the number of jobs created in some months when weather conditions decrease employment.



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**Appendix X: Massachusetts**

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**Massachusetts's  
Comments on This  
Summary**

We provided the Governor of Massachusetts and representatives of oversight agencies with a draft of this appendix on April 17, 2009, and representatives from the Governor's office and the oversight agencies responded that day. In general, they agreed with our draft and provided some clarifying information, which we incorporated. The officials also provided technical suggestions that were incorporated, as appropriate.

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**Staff  
Acknowledgments**

In addition to the contacts named above, Carol L. Patey, Assistant Director; Ramona L. Burton, analyst-in-charge; Kathleen M. Drennan; Salvatore F. Sorbello, Jr.; and Robert D. Yetvin made major contributions to this report.

## Appendix XI: Michigan

### Overview

**Use of funds:** In estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities nationwide will be for health, transportation, and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$701 million in increased FMAP grant awards to Michigan.
  - From January 2008 to January 2009, the state's Medicaid enrollment increased from 1,547,259 to 1,624,245 with the highest share of increased enrollment attributable to two population groups: (1) children and families and (2) disabled individuals.
  - As of April 1, 2009, Michigan has drawn down about \$463 million—which represents funds drawn down for two quarters—or 66.1 percent of its initial increased FMAP grant awards.
  - Officials plan to use funds made available as a result of the increased FMAP to cover increased caseloads, offset general fund shortfalls, ensure compliance with prompt payment provisions, maintain existing populations of Medicaid recipients, avoid eligibility restrictions, increase provider payments, maintain current levels of benefits, and avoid benefit cuts.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Michigan was apportioned about \$847 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009 the U.S. Department of Transportation had obligated \$110.8 million for 27 Michigan projects.
  - As of April 13, 2009, the Michigan Department of Transportation had advertised 16 projects for competitive bid totaling more than \$41 million. These projects included resurfacing I-196 in Grand Rapids and M-13 in Genesee County.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Michigan was allocated about \$1.1 billion from the U.S. Department of Education's initial release of these funds on April 2, 2009.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. Michigan plans to submit its application on or after May 15, 2009, once it completes its review of all program priorities for which it intends to use stabilization funds.
  - Michigan Department of Education officials told us they consulted with local education agencies to develop plans and establish priorities for the use of State Fiscal Stabilization Fund funds that were consistent with the state's priorities, policies and programs, such as increasing support for the lowest performing schools.

## Appendix XI: Michigan

Michigan is receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); the Individuals with Disabilities Education Act (IDEA), Part B; Federal Transit Administration Transit Grants; and the Edward Byrne Justice Assistance Grants. These are described in this appendix.

**Safeguarding and transparency:** All of the state and local agency officials we interviewed indicated they plan to use existing systems to separately identify and track Recovery Act funding. State officials were confident that their existing processes, modified to incorporate specific Recovery Act codes, would be sufficient to allow them to separately account for funds as required by the act. However, officials were uncertain whether local entities have the capacity to similarly track federal funds that go directly to local entities rather than through the state.

Michigan also plans to continue using existing internal controls and processes to provide assurances over Recovery Act spending. Michigan has established a new Recovery Office to, among other things, provide oversight and enhance transparency over the availability and use of funds and maintain a Web site on Michigan's Recovery and Reinvestment Plan ([www.michigan.gov/recovery](http://www.michigan.gov/recovery)). Michigan's existing processes also include ongoing risk-based self-assessments of controls by major state agencies that are next due on May 1, 2009. However, these assessments are limited to state agencies. In addition, the state Auditor General has identified material weaknesses in two key departments that have received Recovery Act funds—Michigan's Department of Human Services and Department of Community Health. The state Auditor General plans to continue working on a biennial basis, reviewing and reporting on about one-half of the state agencies each year. The state Auditor General's oversight responsibilities do not include efforts to ensure accountability over federal funds going directly to localities. For example, the U.S. Department of Education's Inspector General identified weak internal controls that resulted in problems in how the city of Detroit school district used federal funds for programs under Title I of ESEA.<sup>1</sup> Specifically, its July 2008 report found that Detroit Public Schools, among other things, did not always properly support compensation charges against ESEA Title I funds. Detroit Public

<sup>1</sup>U.S. Department of Education, Office of Inspector General, *The School District of the City of Detroit's Use of Title I, Part A Funds Under the No Child Left Behind Act of 2001*, ED-OIG/A05H0010 (July 2008).

Schools officials told us that in the spring of 2009 they hired new staff to develop corrective action plans for addressing existing internal control weaknesses.

**Assessing the effects of spending:** Michigan officials have some experience in measuring the impact of funds in creating jobs and promoting economic growth. The state plans to rely on experts in economic modeling. The state's financial management system, however, is old and does not have the capability to track impacts, so the state will have to rely upon its agencies for this. State officials also told us that the state information technology group will implement a database system at the end of April 2009 that will support its financial management system in recording the impact of Recovery Act funds.

### Michigan Beginning to Use Recovery Act Funds

Faced with the highest unemployment rate of all the states (as of February 2009), heavy reliance on the deteriorating car manufacturing sector, and declining tax revenue, Michigan officials plan to use Recovery Act funds to address the state's immediate fiscal needs as well as to help develop long-term capacity. From an employment peak in June 2000, Michigan had lost about 520,000 jobs as of December 2008. Unemployment sharply increased from 7.4 percent in February 2008 to 12 percent in February 2009, and several local communities had even higher rates. For example, since domestic auto manufacturing dominates Detroit's economy, the unemployment levels in the city have been consistently higher than in the rest of the state. As of December 2008, the city's jobless rate was 18.6 percent and according to Detroit officials reached nearly 22.8 percent in March 2009. To help address these issues, prior to the enactment of the Recovery Act on February 17, 2009, the federal government provided \$23.7 billion to two auto companies and two financing companies operating in Michigan as part of the Troubled Asset Relief Program.<sup>2</sup>

Michigan has been experiencing declines in state revenues. In January 2009, Michigan reported an expected budget gap of approximately \$1.4 billion for fiscal year 2010. In response, the Governor has proposed budget cuts for fiscal year 2010 of \$670 million in key state programs such as public education, corrections, and community health; \$232 million in

<sup>2</sup>U.S. Government Accountability Office, *Troubled Asset Relief Program: Status of Efforts to Address Transparency and Accountability Issues*, GAO-09-474T (Washington, D.C.: March 11, 2009).

revenue enhancements, such as tax increases and elimination of tax exemptions; and using funds made available as a result of \$500 million in increased FMAP funds to offset the budget gap.

In March 2009, Michigan's legislature estimated that the state would receive approximately \$7 billion in Recovery Act funding. These estimates show that the majority of Recovery Act funds would support education (36 percent), Medicaid (32 percent), and transportation (14 percent), with smaller amounts of funding available for other programs (18 percent).

Michigan has begun to use some of its Recovery Act funds, as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>3</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery act.<sup>4</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their

<sup>3</sup>Recovery Act, div.B, title V, § 5001.

<sup>4</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

Medicaid programs, and states have reported using these available funds for a variety of purposes.

Under the Recovery Act, Michigan's FMAP will increase to at least 69 percent, up from 58 percent in 2008. From January 2008 to January 2009, the state's Medicaid enrollment increased from 1,547,259 to 1,624,245, with the highest share of increased enrollment attributable to two population groups: (1) children and families and (2) disabled individuals. As of April 1, 2009, Michigan has drawn down \$463 million, 66.1 percent, of its awards to date.<sup>5</sup> Michigan officials indicated that they will use funds made available as a result of the increased FMAP to cover increased caseloads, offset general fund shortfalls, ensure compliance with prompt payment provisions, maintain existing populations of Medicaid recipients, avoid eligibility restrictions, increase provider payments, maintain current levels of benefits, and avoid benefit cuts.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation funding, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Michigan has submitted these certifications.

As of April 16, 2009, the U.S. Department of Transportation had obligated \$110.8 million for 27 Michigan projects.<sup>6</sup> On March 31, 2009, the Governor signed state legislation authorizing the use of federal Recovery Act funds

<sup>5</sup>Michigan received increased FMAP grant awards of \$700.5 million for the first three quarters of federal fiscal year 2009.

<sup>6</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

for transportation projects that are expected to create about 25,000 jobs.<sup>7</sup> As of April 13, 2009, the Michigan Department of Transportation (MDOT) had advertised 16 projects totaling more than \$41 million for competitive bidding. These projects included resurfacing I-196 in Grand Rapids and M-13 in Genesee County. Michigan was apportioned about \$982 million for transportation projects, including \$847 million for highway infrastructure investment projects and \$135 million for urban and rural transit projects. MDOT was apportioned about 75 percent of Recovery Act highway infrastructure investment funds and remaining funds will be suballocated to metropolitan, regional, and local organizations.

MDOT identified 178 road and bridge projects that would, among other things, improve road pavement conditions on 1,300 lane miles of roadways, add lanes to four major roads to reduce congestion, and perform work on 112 bridges, of which 41 are structurally deficient. According to MDOT officials, the priority was to select shovel-ready projects that could be initiated and completed quickly. In Michigan, Recovery Act funds are being used primarily to fund transportation projects in fiscal year 2009 that were originally scheduled to begin in fiscal year 2010 or beyond, as well as some projects that had been identified but had no source of funding. MDOT officials told us they intend to complete selecting and approving specific road and bridge projects to be funded with Recovery Act money by May 1, 2009.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take action to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Michigan's initial SFSF allocation is \$1.1 billion. The Recovery Act provided State Fiscal Stabilization Funds to increase funding for education over the next several years and avoid program cuts and teacher layoffs in fiscal year 2010. The amount of funding for each of the initiatives has not

<sup>7</sup>Michigan's fiscal year 2008-2009 Supplemental Appropriations, Federal American Recovery and Reinvestment Act (Transportation), Public Act 3 of 2009.

yet been determined. Michigan plans to submit its application for SFSF funds on or after May 15, 2009, once the state completes its review of all program priorities for which it intends to use stabilization funds. Michigan Department of Education officials told us they consulted with local education agencies to develop plans and establish priorities for the use of SFSF funds that were consistent with the state's priorities, policies, and programs, such as increasing support for the lowest performing schools.

**U.S. Department of Education ESEA Title I and Individuals with Disabilities Education Act (IDEA) Funds:** Michigan Department of Education officials told us that although the amount of funding for each of these two initiatives has not yet been determined they anticipate that Recovery Act funds for ESEA Title I (\$390 million) and IDEA (\$426 million) will generally be used to support the same priorities that are funded in part by U.S. Department of Education funds that the state now receives. The state plans to use Recovery Act funds to support specified educational outcomes—reading, mathematics, and other learning proficiencies—and foster enhanced access to education programs for special needs students. Michigan's Department of Education also intends to use Recovery Act funds to support professional development among teachers that can help sustain achievement of educational outcomes beyond the time limits of Recovery Act funding.

**U.S. Department of Justice Edward Byrne Memorial Justice Assistance Grant Program:** Michigan plans to apply for \$67 million in Recovery Act funds for crime control and prevention activities. Michigan Department of Community Health officials told us that about \$41 million of these funds will support, among other things, state efforts to reduce the crime lab backlog, funding for multi-jurisdictional courts, and localities' efforts regarding law enforcement programs, community policing, and local correctional resources. An additional \$26 million in Recovery Act funds will go directly to localities to support efforts against drug-related and violent crime. On April 13, 2009, Michigan began accepting grant applications from local Michigan jurisdictions for Byrne Justice Assistance grants funding administered by the state and will continue to accept them until May 11, 2009.



## Michigan Is Augmenting Its Approach to Safeguarding and Transparency of Recovery Act Funds but Gaps Exist

All state and local agency officials we interviewed indicated that they plan to use their existing systems to tag and track Recovery Act funding, including increased FMAP funds. State officials were confident that their existing processes for receiving, coding, and monitoring federal funds could be used to separately account for the use of Recovery Act funds as required by the Act. For example, Michigan's Department of Education has used the Michigan Electronic Grants System since 2001 to generate recipient reports on the use of ESEA Title I, IDEA, and State Fiscal Stabilization Funds. According to its officials, Michigan Department Education plans to continue to use the grants system for reporting on recipients' use of Recovery Act funds by creating new accounting codes for Recovery Act funds.

Although state government officials told us they believed that their departments have sufficient capabilities to segregate Recovery Act funds, many expressed less confidence in the capabilities of sub-recipients to separately account for the use of Recovery Act funds. State officials expressed concerns about the capacity of smaller agencies and organizations to separately track and monitor Recovery Act funds. For example, Detroit Public Schools officials told us that the school district has not had a clearly specified process for segregating funds from different funding streams and for how it intends to use Recovery Act funds. According to the officials, in the last several years, the district has commingled ESEA Title I funds with its general funds, making it difficult to track the use of ESEA Title I funds and show that they were used only for allowable expenditures. In addition, according to Detroit Public Schools officials, without improvements to its oversight of these funds, Detroit Public Schools may continue experiencing oversight challenges with respect to Recovery Act funds provided through ESEA Title I and IDEA funding streams. For example, according to a July 2008 report from the U.S. Department of Education's Office of Inspector General, the Detroit Public Schools district, among other things, did not always properly support compensation expenses charged to ESEA Title I funds.<sup>8</sup> District officials told us that in April 2009 they hired new staff to develop corrective action plans for addressing existing internal control weaknesses.

<sup>8</sup>U.S. Department of Education Office of Inspector General: *The School District of the City of Detroit's Use of Title I, Part A Funds Under the No Child Left Behind Act of 2001*, ED-OIG/A05H0010, July 2008.

### Safeguarding Recovery Act Funds

In anticipation of the opportunity to receive additional federal funding and the need to act quickly, Michigan began preparations before the Recovery Act was enacted. For example, the Governor established a working group of executive branch officials from Michigan state agencies and departments, known as Economic Recovery Coordinators (ERC), to plan for the use of anticipated Recovery Act funds.

On February 13, 2009, the Governor established a Recovery Office for coordination of all Recovery Act activities, including communication with stakeholders within and outside the state. The Recovery Office is responsible for helping develop priorities for the use of Recovery Act funds by the state consistent with the objectives of the Recovery Act and with the state's priorities identified to fully maximize the impact of these federal funds.<sup>9</sup> Similarly, Detroit officials told us that they began planning in November 2008 for the receipt of Recovery Act funds and identified over 160 city projects that could be funded by working closely with city departments and community action organizations. Lansing Schools District officials told us that they began planning early for use of Recovery Act funding for the district's 34 schools. The Recovery Office has also been working with state agencies to develop strategies for overseeing and tracking the use of Recovery Act funds to comply with requirements of the act and minimize fraud, waste, and abuse of funds and to help ensure consistent, timely, and accurate compliance with all reporting and certification requirements under the Recovery Act. Michigan is also maintaining a Web site on Michigan's Recovery and Reinvestment Plan ([www.michigan.gov/recovery](http://www.michigan.gov/recovery)).

According to state officials, Recovery Act funds must be appropriated by the state legislature before the state is authorized to spend the money. In addition, the Michigan Senate created a special committee, known as the Senate Federal Stimulus Oversight subcommittee, to oversee Recovery Act funds.

Michigan Department of Management and Budget officials told us that they are prepared to manage Recovery Act funds because they plan to use existing processes for purchasing goods and services. For example, Michigan will use existing processes to obtain competitive bids for

<sup>9</sup>Governor Granholm identified five priorities: (1) create new jobs and jumpstart Michigan's economy, (2) train Michigan workers and educate Michigan students, (3) rebuild Michigan infrastructure, (4) provide assistance for struggling Michigan families, and (5) invest in energy efficiency and renewable energy technologies.

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contracts awarded by state agencies under the Recovery Act in accordance with state law, which state officials described as requiring competitive bids (other than certain exceptions such as emergencies or imminent protection).<sup>10</sup> In January 2009, Michigan created a prequalification program for vendors to provide an inventory of prequalified vendors ready to quickly respond to bids for work that will spend Recovery Act funds. As part of preparing to spend Recovery Act funds, Michigan Department of Management and Budget officials also told us they have been looking at ways to further streamline awarding contracts. Michigan also allows local units of government to join state contracts to leverage the state's negotiating and purchasing power.

### Michigan Using Existing Internal Controls

Michigan will continue to use existing internal controls to provide assurances over Recovery Act spending, including ongoing self-assessments of controls by major state departments that are next due to the state Auditor General on May 1, 2009. The self-assessments include identification of internal controls and programmatic weaknesses and developing and tracking actions taken in response to corrective action plans.

The state Auditor General told us his office will include specific audit procedures to address Recovery Act funding as part of the planned procedures for its ongoing federal Single Audits of state departments which will start again in July 2009. However the state Auditor General does not yet have specific plans to audit Recovery Act funds. The state Auditor General's Single Audit approach is to audit and report on individual state departments. Approximately one-half of Michigan's 18 departments are audited each year, with the audits covering 2 fiscal years of departmental activity.

Recent state Auditor General Single Audit Act reports identified numerous material weaknesses in key state operations that are slated to receive significant amounts of Recovery Act funds. For example, the state Auditor General reported in August 2007 that, for fiscal years 2005 and 2006, Michigan's Department of Human Services did not materially comply with federal program requirements regarding allowed or unallowed costs, subrecipient monitoring, and eligibility. The October 2008 Single Audit report on Michigan's Department of Community Health stated that internal

<sup>10</sup>See Management and Budget Act, Act 431 of 1984, sec. 261.

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controls were not sufficient to ensure the accuracy of financial accounting and reporting and compliance with federal requirements for 10 of 11 major programs.

The Michigan Auditor General's oversight responsibilities do not include most subrecipients<sup>11</sup> that receive federal funding, so any upfront safeguards to track or ensure accountability over Recovery Act funds going directly to localities have not been determined. Officials from Detroit's Office of the Auditor General told us that they intend to audit the use of Recovery Act funds. The superintendent of the Lansing school district told us the district, along with all the other 840 local school districts in the state, contract with independent public accountants to perform annual financial statement audits.

**State Has Identified Staffing and Resource Constraints as a Significant Challenge in Monitoring the Use of Recovery Act Funds**

A lack of staff and uncertainty of funding available under the Recovery Act to oversee the use of federal funds may pose challenges for Michigan. Michigan officials reported that a hiring freeze may not allow some state agencies to hire staff to increase their Recovery Act oversight efforts. Officials with the state's Departments of Community Health and Education and the Lansing School District are concerned about available administrative resources to cover increased oversight activities on the use of Recovery Act funds. For example, the state Department of Community Health said that because it has been downsizing for several years through attrition and early retirement, it does not have sufficient staff to cover its current responsibilities and that further reductions are planned for fiscal year 2010. However, state officials told us that they will take the actions necessary to ensure that state departments have the capacity to provide proper oversight and accountability for Recovery Act funds.

**Michigan Officials Concerned about the Lack of Federal Guidance**

Michigan officials we spoke with in March 2009 wanted additional federal guidance related to state responsibilities and reporting requirements under the Recovery Act and expressed concern about spending funds before they had received such guidance. For example, officials were unclear about the state's responsibilities concerning tracking or reporting on funds that go directly to local entities, such as transportation funding going directly to localities for urban transit. In addition, Michigan Department of

<sup>11</sup>Single Audits performed by the state Auditor General include audit procedures of subrecipients when the subrecipient is a state agency.

## Appendix XI: Michigan

Education officials expressed concern about the lack of guidance from the U.S. Department of Education regarding several aspects of how to manage the receipt, allocation, use, and reporting of Recovery Act funds. In particular, state officials said they had not yet received guidance on tracking funds under IDEA, Part C and were concerned that recipients of grant funds might report information inconsistently. On April 1, 2009, the U.S. Department of Education issued additional guidance on the use of Recovery Act funds.

### Plans to Assess Impact of the Recovery Act Are Preliminary

Michigan may face challenges in assessing the impact of Recovery Act funds because the state's financial management system is old and does not have the capability to track impacts, so the state will have to rely upon its agencies for this. Furthermore, state officials said they are aware of the requirement that the state measure the extent that certain Recovery Act funds create jobs and promote economic growth and have identified prospective participants to estimate the impact of Recovery Act funds. State officials also told us that the state information technology group will implement a database system at the end of April 2009 that will support its financial management system in recording the impact of Recovery Act funds. They told us that the Michigan Economic Development Corporation, universities in the state and other experts in economic modeling are expected to participate in prospective analysis supporting the potential impact of Recovery Act funds on a project basis. Additionally, the Department of Energy, Labor and Economic Growth and the state Treasurer will also be involved in analysis related to the impact of Recovery Act's funds.

### Michigan's Comments on This Summary

We provided the Governor of Michigan with a draft of this appendix on April 17, 2009. Michigan's Recovery Czar responded for the Governor on April 20, 2009, stating that staff in the Michigan Governor's office and the Michigan Economic Recovery Office have reviewed the draft appendix and, in general, agree with its overview of the state's preparations for receiving and spending Recovery Act funding. These officials provided technical comments on the draft which were incorporated, as appropriate.

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Acknowledgments**

In addition to the contacts named above, Robert Owens, Assistant Director; Jeffrey Isaacs, Analyst-in-Charge; Manuel Buentello; Leland Cogliani; Anthony Patterson; and Mark Ward made major contributions to this report.

## Appendix XII: Mississippi

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 1, 2009, Centers for Medicare and Medicaid Services (CMS) had made about \$225.5 million in increased FMAP grant awards to Mississippi.
  - As of April 1, 2009, the state had drawn down \$114.1 million, or just more than 50 percent of its initial increased FMAP grant awards.
  - State officials reported that they plan to use funds made available as a result of the increased FMAP to cover their increased Medicaid caseload and to offset expected state budget deficits due to lower general fund revenue collections.
- ✓ **Transportation—Highway Infrastructure Investment**
  - On March 2, 2009, the U.S. Department of Transportation apportioned Mississippi about \$355 million for highway infrastructure investment.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated approximately \$137 million for 32 Mississippi projects.
  - As of April 1, 2009, Mississippi had signed contracts for 10 projects totaling approximately \$77 million. The Mississippi Department of Transportation (MDOT) used a competitive and transparent process to select projects. These projects include activities such as road construction and road maintenance.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - On April 2, 2009, the U.S. Department of Education allocated Mississippi about \$321 million from the initial release of these funds.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements or will be able to comply with waiver provisions and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. Mississippi plans to submit its application for state fiscal stabilization funds after it receives and reviews the final program guidance.
  - Mississippi expects to use these funds to help restore funding for elementary, secondary, and public higher education to prior levels in order to minimize reductions in education services in fiscal years 2009, 2010, and 2011. The state does not foresee having leftover funds for additional subgrants to local education agencies.

Mississippi is receiving additional Recovery Act dollars to fund other programs, including employment and training programs under the Workforce Investment Act, capital and management activities under the Public Housing Capital Fund, and gap financing for low-income housing tax credit projects under the Taxpayer Credit Assistance Program. The status of Mississippi's plans for using these funds is described throughout this appendix.

**Safeguarding and transparency:** The State Auditor's office has taken steps to ensure accountability. For example, the office hosted a meeting with state agency heads to discuss accountability requirements and expectations, and the office plans to conduct training seminars on accounting for and controlling the use of Recovery Act funds. In addition, officials with the auditor's office said Mississippi plans to add special accounting codes to the statewide accounting system in order to track the expenditure of Recovery Act funds. The state also plans to publicly report Recovery Act spending that state agencies receive directly. State officials noted that the statewide accounting system would not capture those funds that the federal government allocates directly to local and regional governmental organizations, nonprofit organizations, or higher education entities. According to the Governor's office, the state is developing a framework that would require these entities to report Recovery Act revenues and expenses to a central website.

**Assessing the effects of spending:** According to state officials, they are waiting for the federal government to provide more specific guidance for measuring job creation and retention. For example, the officials noted that the federal government's Office of Management and Budget (OMB) should provide more guidance for estimating job creation and retention.

### Mississippi Beginning to Use Recovery Act Funds

Mississippi has begun to use some of its Recovery Act funds, as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal



matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

Under the Recovery Act, Mississippi's FMAP will increase to 83.62 percent, an increase of 7.33 percentage points over its fiscal year 2008 FMAP. As of April 1, 2009, Mississippi had drawn down \$114.1 million or just more than 50 percent of its initial increased FMAP grant awards. Mississippi officials plan to use funds made available as a result of the increased FMAP to cover their increased Medicaid caseload and to offset expected state budget deficits due to lower general fund revenue collections, avoiding cuts in services. Mississippi officials indicated that simplifications to CMS expenditure reporting systems are needed to automatically generate the increased FMAP applicable to qualifying expenditures. Officials also reported a need for CMS guidance regarding programmatic changes that were made to its Family Planning Waiver since July 1, 2008, and whether these changes affect the state's ability to draw down the increased FMAP.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation program, which apportions money to states to construct and maintain eligible highways and for other surface transportation

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

projects that could affect highways. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Mississippi's Governor provided this certification in a letter dated March 17, 2009. The Governor noted that transportation spending authority in Mississippi is granted annually by the state Legislature to the Mississippi Department of Transportation (MDOT), which operates under the guidance of independently elected transportation commissioners. As such, MDOT's Executive Director also provided this certification.

As of April 1, 2009, MDOT had signed contracts for 10 projects totaling approximately \$77 million.<sup>3</sup> The agency used a transparent and competitive process for awarding contracts for these projects. MDOT issued an advance notice on its Web site to inform contractors of the opportunity to bid on the projects. Furthermore, MDOT used cost as a key criterion for awarding contracts. MDOT awarded the contract to the lowest bid, provided that the lowest bid did not exceed the state's cost estimate for the project by more than 10 percent. These projects include the expansion of State Route 19 in eastern Mississippi into a four-lane highway. This project fulfills part of MDOT's 1987 Four-Lane Highway Program, which seeks to link every Mississippian to a four-lane highway within 30 miles or 30 minutes. In addition, MDOT plans to upgrade a section of a major road, US-78, which runs across northern Mississippi. An MDOT official anticipated the project would have major economic benefits for Mississippi.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF), to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each

<sup>3</sup>As of April 16, 2009, the U.S. Department of Transportation had obligated \$137 million for 32 Mississippi projects. For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

## Appendix XII: Mississippi

state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Mississippi's initial SFSF allocation is about \$321 million. The Recovery Act specifies that 81.8 percent is to be used for support of elementary, secondary and postsecondary education, and early childhood programs. The Recovery Act also authorizes the Governor to use 18.2 percent of these funds for "public safety and other government services," which may include education. Mississippi's Governor has not yet announced specific plans for the use of these other government services funds. According to state education officials, Mississippi will file its application for these funds after receiving and reviewing sufficient guidance. The funds will be appropriated to the state education agencies by the Mississippi State Legislature when it returns to session later this spring. The funding is expected to be used to stabilize education budgets in fiscal years 2009, 2010, and 2011 to help avoid reductions in education services. Restoring funding in those years to required levels is expected to consume all of the stabilization funds to be received by the state.

#### Mississippi Is Planning for Recovery Act Funding

Mississippi began planning for how the state would provide oversight of Recovery Act funding in February 2009. Officials from the Governor's Office said that the state did not establish a new office to provide statewide oversight of Recovery Act funding, in part because they did not believe that the act provided states with funds for administrative expenses—including additional staff. The Governor's Director of Federal Policy is serving as the stimulus coordinator for the state with support from a loaned executive from a statewide business development association. The stimulus coordinator told us she met individually with state agency heads to discuss their plans for spending funds allocated under the Recovery Act. In late March 2009, the Governor submitted a letter certifying that Mississippi would request funds available under the Recovery Act and such funds will be used to create jobs and promote economic growth. The Governor added in the certification letter that the state would continue to examine the various guidelines and fund-specific requirements associated with the Recovery Act funds. In April 2009, the Governor hosted a Mississippi Stimulus Summit where state agency heads provided information on the detailed steps that were already being taken or were planned regarding the use of Recovery Act funds. Finally, the Governor established a state stimulus Web site ([www.stimulus.ms.gov](http://www.stimulus.ms.gov)) to

provide information to the public on the Recovery Act funding received by the state.

**Addressing State's Fiscal Challenges Is Mississippi's Goal for Using Recovery Act Funding**

Mississippi officials plan to use the anticipated \$2.8 billion in Recovery Act funding to address fiscal challenges the state has experienced due to a weakened economy. State officials reported that Mississippi entered a recession in late 2008. One indicator of Mississippi's weakened economy is the state's unemployment rate, which was 8.7 percent in January 2009 compared with 6.9 percent in June 2008. The state's weakened economy has also resulted in lower-than-expected tax revenues for the state's current fiscal year. According to the Governor, Mississippi's Revenue Estimating Committee projected that the state's fiscal year 2009 general fund revenue will fall \$301 million, or 5.9 percent, short of expectations. In response to anticipated budget shortfalls, the Governor made two cuts to most state agency budgets. In November 2008, the Governor cut most agency budgets by 2 percent, or \$42 million. In January 2009, the Governor cut state agencies' budgets by an additional \$158.3 million, bringing the total cuts to date for the fiscal year to \$200 million. Each agency or department received a budget cut of up to 5 percent (see table 8).<sup>4</sup> Although the Governor anticipated that Congress would pass a stimulus package, he ordered the cuts in agency budgets to comply with state law that requires a balanced budget for the fiscal year, which ends on June 30.

<sup>4</sup>According to Mississippi officials, under Mississippi law, the Governor may cut any department or agency by 5 percent of its appropriation; however, the Governor cannot cut any department or agency by more than 5 percent until every department and agency has been cut by 5 percent.

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**Table 8: Budget Reductions for Selected State Agencies in Mississippi for Fiscal Year 2009**

Selected agency	Appropriations for fiscal year 2009	Total budget cuts in fiscal year 2009	Percentage change during fiscal year 2009
Corrections	\$328,180,918	\$16,409,046	-5.0
Highway Safety Patrol	48,440,661	2,422,033	-5.0
Judiciary and Justice	63,799,714	3,189,985	-5.0
Economic Development	25,748,751	1,287,438	-5.0
Higher Education	961,063,754	46,649,166	-4.9
Fiscal Affairs	72,724,225	3,577,428	-4.9
Hospitals and Hospital Schools	278,480,866	13,226,449	-4.7
Public Education	2,517,323,677	92,021,567	-3.7
Public Health	61,264,961	1,705,331	-2.8
Social Welfare	692,477,684	6,603,119	-1.0

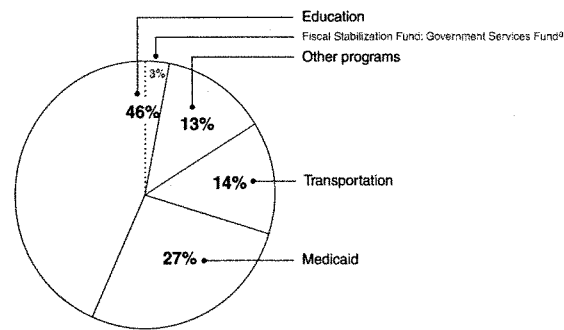
Source: GAO analysis of Mississippi Department of Finance and Administration data.

To mitigate the impact of economic fluctuations on state revenues, Mississippi has historically set aside 2 percent of projected revenues into a budget stabilization fund. In 2008, however, the state did not set aside any revenues for this fund, which made available an additional \$100 million for Mississippi's 2009 fiscal year budget. Going forward, Mississippi faces budgetary challenges for fiscal year 2010. According to the Governor, the state's Revenue Estimating Committee projects that Mississippi's revenues will be \$402.7 million, or 7.9 percent, short of expectations. State officials anticipate that the recession will increase the demand for certain government services, including unemployment benefits, Medicaid, food stamps, and rental assistance. Some Mississippi officials believe that the state's recession could continue through fiscal year 2012.

Most of the Recovery Act funds that Mississippi will receive are directed toward education, Medicaid, and transportation programs (see fig. 9). According to the Governor's office, state law provides for state agencies to escalate their spending plans to account for federal funds received under the Recovery Act. State officials also told us that the Legislature was considering adding further escalation language to the current fiscal year's appropriations bills that would authorize state agencies to spend any Recovery Act funds received. The Legislature normally conducts its regular session between the beginning of January and the end of March. However, the Legislature recessed early during the 2009 regular session in

part because of uncertainty regarding how the state's portion of Recovery Act funds should be spent. The Legislature plans to reconvene in early May 2009 to complete its work on the state's fiscal year 2010 budget.

**Figure 9: Estimated Allocation of Mississippi's Recovery Act Funding by Major Programs**



Source: GAO analysis of data provided by Mississippi Joint Committee on Performance Evaluation and Expenditure Review.

\*A portion of the Fiscal Stabilization Fund is allocated for the Government Services Fund. The Government Services Fund may be used for public safety and other government services, including assistance for elementary and secondary education and public institutions of higher education.

### Mississippi Has an Accounting System to Track Recovery Act Spending

Officials with the State Auditor's office told us that special accounting codes will be added to the Statewide Automated Accounting System (SAAS) in order to track the expenditure of Recovery Act funds. The state also plans to publicly report Recovery Act spending that state agencies receive directly. However, state officials noted that SAAS would not track Recovery Act funds allocated directly to local and regional governmental organizations, nonprofit organizations, or higher education entities. For example, cities with a population of more than 50,000 residents can apply directly to federal agencies for certain programs, such as Community Development Block Grants. In addition, Mississippi has 10 regional planning and development districts that may receive funding directly from federal agencies. Finally, Mississippi localities may receive Recovery Act funds directly from the Appalachian Regional Commission or Delta Regional Authority, federally chartered regional commissions charged

with promoting economic development in certain parts of the state. According to the Governor's office, the state is developing a framework that would require these entities to report Recovery Act revenues and expenses to a central website.

#### Some State Agencies Have Made Spending Decisions for Recovery Act Funds

A few state agencies have made spending decisions for Recovery Act fund apportionments received:

- The Mississippi Department of Employment Security (MDES) received about \$40.7 million in Recovery Act funding for adult, dislocated worker, and youth activity programs under the Workforce Investment Act. MDES officials told us they planned to use the youth activity funding to provide summer youth programs across the state.
- The Jackson Public Housing Authority received a \$1.1 million allocation to its Public Housing Capital Fund from the Department of Housing and Urban Development (HUD) for capital and management activities, including modernization and development of public housing projects. The officials told us they planned to use the Recovery Act allocation to fund projects already included in their 5-year Capital Fund Plan—for instance, one project will redevelop housing in Jackson's North Midtown Community.
- The Mississippi Home Corporation (MHC) was allocated approximately \$21.9 million to provide additional gap financing to Low Income Housing Tax Credit (LIHTC) projects under the Taxpayer Credit Assistance Program (TCAP). MHC officials told us they had provided an initial notice to developers of LIHTC projects in the state about the additional funding provided under the Recovery Act for the TCAP but were waiting for HUD to issue final guidance before releasing details on their plans for administering the Recovery Act funding.

#### State Auditor Coordinating Plans for Safeguards and Controls

The State Auditor's office has taken and plans to take a number of steps to establish accountability. For example, in March 2009 the office hosted a meeting with staff from state agencies that are expected to receive Recovery Act funds to discuss accountability requirements and expectations. The office is planning to conduct training seminar for local officials and others concerned about accounting for and controlling the use of Recovery Act funds. Overall, the State Auditor believes the state has adequate controls for the use of Recovery Act funds but is concerned that the funding of new programs and the significant increase in funding of

current programs will stress the control system. In addition to the State Auditor, a legislative oversight committee and internal audit offices within each agency may provide oversight of Recovery Act funds. For example, the legislative committee staff in March 2009 said they began tracking the Recovery Act and the state's Recovery Act-related legislation and funding provided to Mississippi.

Mississippi's most recent Single Audit Act findings highlight two material weaknesses in internal control over financial reporting at one state agency that will receive Recovery Act funds. In its Single Audit report for fiscal year 2008, the State Auditor found that the Mississippi Department of Employment Security did not record the tax liens receivable account and corresponding Unemployment Insurance Premiums revenue account on the department's financial statements in accordance with generally accepted accounting principles. As a result, the State Auditor proposed, and management made an audit adjustment of, approximately \$35.5 million to properly state the department's current year financial statements. In addition, the State Auditor found that the department's internal controls over its tax lien receivable system were inadequate, and management proposed audit adjustments totaling approximately \$6.4 million to properly state the department's tax lien receivables. The State Auditor also identified one material weakness in internal control over compliance at the Mississippi Department of Human Services for the department's failure to verify and document compliance with the Davis-Bacon Act requirements for the Social Services Block Grant, which could result in questioned costs and funds due back to the federal granting agency.

#### Resources for Conducting Oversight Are Limited

State officials stated that the Recovery Act does not provide funding to oversight entities, but the federal government expects states to ensure accountability and transparency over expenditures. For example, officials from the State Auditor's office told us they had experienced significant staff turnover in recent years and relied on less-experienced staff to conduct audit work. In addition, the Lieutenant Governor expressed concern about whether the State Auditor could be funded to conduct additional Recovery Act-related auditing responsibilities, as was done for Hurricane Katrina related oversight. Officials from the State Auditor's office added that they normally charged the audit agency for the cost of audit services provided, but they were not sure whether Recovery Act funds could be used for this purpose. The State Auditor noted that the office would like to hire certified public accounting firms to conduct Recovery Act oversight work rather than increase staff. Further, the



officials noted that OMB should provide guidance regarding state level oversight, auditing, and administrative costs—such as how costs should be paid for and with what funds.

The legislative oversight committee also expressed concerns about the capabilities of the State Auditor's office and some state agency internal audit functions. For example, in a recent report, the committee noted that low staffing levels and high turnover in the office's Department of Audit's Financial and Compliance Audit Division had resulted in a decreased experience level of audit staff and reduced institutional knowledge to use in forming auditor judgment.<sup>6</sup> In addition, the committee noted there were limitations in the internal audit functions of some state agencies—for instance, state law required 19 agencies to establish an internal audit function; 13 had done so as of December 2008. Further, the committee reviewed the internal audit functions of 8 agencies and found that most focused on reviewing agency programs rather than testing internal controls. Finally, the committee found that the Executive Director for these agencies reviewed and approved the plans for their internal audit function, but this could limit the internal auditor's freedom to determine the internal controls tested and programs reviewed.

#### Assessing the Impact of Recovery Act Funds Requires Clear Federal Guidance

Officials from the State Auditor's office recommended that the federal government provide specific guidance for reporting on the use of Recovery Act funds to support job creation or retention because the reliability of such estimates depends critically on using a solid methodology. Furthermore, the officials recommended that OMB provide a clear definition of time-limited, part-time, full-time, and permanent jobs. Another concern was how to report on jobs created from the use of funds for programs, such as unemployment, food stamps, and Medicaid. These funds make up a large portion of the Recovery Act funding, but, according to state officials, the purpose of these programs is not job creation and retention.

The State Auditor's office also expressed concerns about data reliability. For example, staff noted that standardization of data was lacking and the various decentralized reporting mechanisms, while certainly cheaper and

<sup>6</sup>Mississippi Joint Legislative Committee on Performance Evaluation and Expenditure Review, *Report to the Mississippi Legislature #518, Enterprise Mississippi: A Vision for State Government* (Jackson, Miss., Dec. 9, 2008).

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less burdensome on state agencies, will not likely provide meaningful data on the impact of Recovery Act funds. Additionally, the staff noted that, if state agencies require their subrecipients to provide nonstandardized and nonuniform data, it will be difficult to identify trends at the state level. They also expressed concern that decentralized reporting would bypass the state-level efforts of accountability. Ultimately, they said state-level, centralized reporting using standardized and uniform data collection elements would be beneficial for state and federal oversight and would raise both the actual and perceived level of accountability.

As an example of state efforts to assess the impact of Recovery Act funds, MDOT hired a contractor to conduct an economic impact analysis of projects MDOT had preselected to receive Recovery Act funding. According to one of the contractor's staff, these projects were preselected on the basis that they were "shovel ready" during the first 90 days of the state receiving stimulus funds. The contractor used a forecasting model to measure the impact that an estimated \$726 million in transportation stimulus funding would have on the state of Mississippi with regard to increased economic spending and the number of jobs from 2009 through 2011.<sup>4</sup>

### Mississippi's Comments on This Summary

We provided the Governor of Mississippi with a draft of this appendix on April 17, 2009. The Director of Federal Policy, who serves as the stimulus coordinator, responded for the Governor on April 20, 2009. The official provided technical suggestions that were incorporated, as appropriate.

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### Staff Acknowledgments

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<sup>4</sup>According to the contractor, the REMI model (Regional Economic Models Inc.) is a forecasting model that determines the economic impacts of transportation developments by identifying the interrelationships and ensuing impacts in five major sectors of the economy: output, production and labor supply; labor and capital demand; wages, costs and prices; and market share.

## Appendix XIII: New Jersey

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

#### ✓ Medicaid Federal Medical Assistance Percentage (FMAP) Funds

- As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$550 million in increased FMAP grant awards to New Jersey. As of April 1, 2009, the state has drawn down \$362.2 million, which is almost 66 percent of its awards to date.
- Officials stated that the funds made available as a result of the increased FMAP allow the state to cover the increase in caseload and maintain current populations and benefits. In addition, these funds will help balance the state's budget and allow the state to eliminate premiums for children in families with incomes less than 200 percent of the federal poverty level in New Jersey's State Children's Health Insurance Program.

#### ✓ Transportation—Highway Infrastructure Investment

- New Jersey was apportioned about \$652 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation. As of April 16, 2009, the U.S. Department of Transportation had obligated \$280.8 million for 12 projects. Under the Recovery Act, highway funds are reimbursable, and New Jersey will receive funds after all or part of each project is completed.
- As of April 16, 2009, the New Jersey Department of Transportation (NJDOT) had advertised competitive bids on 10 projects totaling about \$269.5 million. New Jersey has determined that it can meet Recovery Act requirements for obligating highway infrastructure investment funds.
- These projects included road improvements, pavement and signal rehabilitation, bridge deck repairs, and major design elements for major projects.

#### ✓ U.S. Department of Education State Fiscal Stabilization Fund (SFSF)

- New Jersey was allocated about \$891 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
- Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. State officials estimated that most of the SFSF funds will have an impact on the state's fiscal year 2010 budget, which will start on July 1, 2009. As of April 16, 2009, New Jersey had not applied for SFSF funds.
- State officials stated that, pending a New Jersey Supreme Court decision on the state's new education funding formula, the SFSF funds for primary education would follow that formula. The state's use of SFSF funds for higher education is unclear. State officials are currently trying to determine what portion of these funds will be allocated to higher education. New Jersey expects to make that determination in late April.

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New Jersey is also receiving additional Recovery Act funds under other programs, such as transit capital assistance and fixed guideway modernization funds, Edward Byrne Memorial Justice Assistance Grants, and housing capital assistance. The status of plans for using these funds are described throughout this appendix.

**Safeguarding and transparency:** New Jersey plans to use several entities to oversee its Recovery Act funds. The Governor has established a state Recovery Accountability Task Force to coordinate and review how state and local agencies use Recovery Act funds as well as provide guidance and best practices for project selection and internal controls, among other things. The state has several accountability agencies that will undertake different aspects of Recovery Act oversight. New Jersey's agencies are adding capabilities to their accounting systems to track Recovery Act funds. Although New Jersey will publicly report the state's Recovery Act spending, state officials said they might not be aware of all federal funds sent directly to other entities, such as public housing authorities. State officials have some concerns about the use of some Recovery Act funds, such as by independent local entities in the state, and they are developing some strategies to mitigate those risks.

**Assessing the effects of spending:** New Jersey state agencies are in the early stages of developing plans to assess the effects of Recovery Act spending. Different state and local agencies will have different ways of collecting or estimating jobs created or retained. New Jersey is planning to develop a methodology to collect this data but is waiting to see what federal guidance requires.

### New Jersey Beginning to Use Recovery Act Funds

New Jersey has begun to use some of its Recovery Act funds, as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008,

and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, New Jersey has drawn down \$362.2 million in increased FMAP grant awards, which is almost 66 percent of its awards to date.<sup>3</sup> New Jersey officials reported that they plan to use funds made available as a result of the increased FMAP to offset state general fund deficits, cover the state's increased Medicaid caseload and maintain current populations and benefits.<sup>4</sup> This funding will also be used to help ensure that the Medicaid prompt payment requirements are met.<sup>5</sup> Additionally, state officials noted that the funds made available as a result of the increased FMAP are allowing them to eliminate premiums for children in families with incomes less than 200 percent of the Federal Poverty Level in New Jersey's State Children's Health Insurance Program

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the effective date of the Recovery Act was February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

<sup>3</sup>As of April 3, 2009, New Jersey received increased FMAP grant awards of \$549.8 million for the first three quarters of federal fiscal year 2009.

<sup>4</sup>From January 2008 to January 2009, the state's Medicaid enrollment increased from 750,529 to 771,156, with increased enrollment mostly attributable to two population groups: (1) children with families, and (2) individuals who are blind or disabled.

<sup>5</sup>Under the Recovery Act, to be eligible for the increased FMAP, states must comply with prompt pay requirements, which require states to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt. 42 U.S.C. § 1396(a)(37)(A); Recovery Act, div. B, title V, § 5001(f)(2).

(SCHIP).<sup>6</sup> This will help the state retain children in SCHIP who would otherwise be terminated from the program for nonpayment of premiums.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects that could affect highways. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of highway spending and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. New Jersey provided these certifications but noted that the state's level of funding was based on the best information available at the time of the state's certification.<sup>7</sup>

At the Governor's direction, NJDOT had begun planning for a federal stimulus package for federal-aid eligible highway projects in November 2008. NJDOT originally developed a list of highway projects worth about \$1.4 billion, which was pared down to meet the actual apportioned amount. NJDOT selected 40 total projects that it could deliver as quickly as possible. As of April 16, the U.S. Department of Transportation had obligated \$280.8 million for 12 New Jersey projects.<sup>8</sup> The projects that were selected concentrated mainly on replacing in-kind projects that require little or no environmental clearance or extensive design work, such as pavement and signal rehabilitation and highway bridge painting and deck replacement. Of the 40 projects selected, 5 are in the design stage, while the rest are in the construction or right-of-way acquisition phases. NJDOT staff indicated they were allocating over a third of their

<sup>6</sup>The annual income for a family of four at 200 percent of the Federal Poverty Level is \$44,100.

<sup>7</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>8</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

Recovery Act transportation funding to 3 large projects, including one in an economically distressed area. As of April 16, 2009, 10 projects totaling about \$269.5 million have been put out for bid through a competitive process. NJDOT officials estimate that Recovery Act funds will save the state about \$100 million in interest charges over 12 years for one of the selected projects, as the state will not have to borrow to start and complete it. Not all of the selected projects were on the State Transportation Improvement Plan (STIP), but New Jersey, in consultation with the Federal Highway Administration, amended its STIP to include all of the selected projects.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF), to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

The state expects to receive \$891.4 million in SFSF funds, about 82 percent of which is for education and about 18 percent of which is for the state to use for "public safety and other government services." State officials said that, pending a New Jersey Supreme Court decision on the state's new education funding formula, the SFSF funds for primary education would follow that formula. The state's use of SFSF funds for higher education is unclear. The Governor's Chief of Staff stated that New Jersey is currently trying to determine what portion of the SFSF education and other government services funds will be used for higher education and will not submit its application for SFSF funding until it completes this determination. New Jersey expects those determinations to be made sometime in April. The state expects that the receipt of stabilization funds will help balance its fiscal year 2009 budget and avoid layoffs or tax increases.

New Jersey state education officials said in March that the lack of clear, specific guidance from Education limited their ability to provide guidance to local institutions. As a result, school district officials we interviewed in Newark and Trenton in late March stated that they are waiting for state officials to tell them what their allocations are for each of the federal Recovery Act education programs. The timing of the federal and state guidelines for these funds are important as the local schools districts are

currently planning their upcoming fiscal year budgets and would like to know how the Recovery Act funds would complement their upcoming school spending. On April 1, 2009, Education issued guidance to the states on how Recovery Act funds could be used for education. State officials are continuing to review the guidance and on April 16, 2009, issued guidance to local school districts outlining each district's allocation of additional funds made available under the Recovery Act for programs authorized under Title I of the Elementary and Secondary Education Act and the Individuals with Disabilities Education Act.

**Transportation—Urban/Rural Transit Capital Assistance and Fixed Guideway Modernization Grants:** New Jersey Transit (NJT), the primary public operator of bus and commuter rail transit lines in the state, was apportioned all of the Recovery Act funds for transit for New Jersey, which amounted to about \$425 million in three pre-existing federal transit programs. NJT has selected 15 projects that will use Recovery Act funds, all of which were on their 20-year capital plan. About 70 percent of the funds are allocated to capacity expansion and improvement projects, with the remainder allocated to maintenance projects, as its regular funds are concentrated on safety, security and maintenance needs. According to NJT officials, NJT can move quickly to use these funds as the Federal Transit Administration (FTA), through its preaward authority, will reimburse the agency for funds expended for the selected projects, even though the funding for those projects has not yet been obligated by the FTA. The largest allocation of NJT's Recovery Act funds (\$130 million) will be used toward designing and undertaking some construction activity for new train tunnels under the Hudson River. The tunnels are expected to double the number of NJT trains going into and out of New York City.

**Housing and Urban Development—Housing Capital Assistance:** HUD allocated approximately \$104 million to 86 public housing authorities in New Jersey for capital and management activities, including modernization and development of public housing developments. Officials from the Newark Housing Authority (NHA), which is receiving an allocation of about \$27.4 million, told us they planned to use the allocation to fund projects already included in their 5-year capital plan—including rehabbing 700 vacant units and 300 occupied units—which will generate income and additional HUD subsidies to NHA and provide new and improved affordable units for additional families.



**Justice—Edward Byrne Memorial Justice Assistance Grants:** State officials expect to receive a Recovery Act allocation of \$48 million from the Byrne Justice Assistance Grant Program.<sup>9</sup> Local law enforcement officials stated that this program may provide for some additional facilities and other law enforcement equipment. For example, the Trenton Police Department is planning to use its Byrne Justice Assistance Grant funds on projects that will enhance its crime reduction efforts by sharing information with Mercer County's Prosecutor's Office and enhancing the department's forensic crime analysis capabilities. In contrast, according to Newark's Chief of Police, the amount of Byrne Justice Assistance Grants allocated to the Newark Police Department may be sufficient to provide some new equipment but not fund a major capital program.

**New Jersey's Plans for Spending Recovery Act Funds Are Forming As Funds Are Being Distributed**

New Jersey revenues for fiscal year 2009 fell short of expectations by about \$3 billion. As a result, New Jersey had to rebalance the state's budget by cutting spending and taking personnel actions in January and February 2009 before the Recovery Act was enacted. In addition, as part of its actions in February, the state used \$450 million of its \$600 million surplus.<sup>10</sup> New Jersey's Office of Management and Budget is accounting for Recovery Act funds that come into state agencies, but there is no concerted effort to independently aggregate estimates of total funding across state agencies.<sup>11</sup> As of April 3, 2009, the state had received about \$583.8 million in Recovery Act funds, mainly for increased FMAP grant awards and unemployment insurance. Other funds have been allocated but are not yet available, such as for some education and energy efficiency programs.

<sup>9</sup>The Byrne Justice Assistance Grant Program supports a broad range of activities to prevent and control crime and may be used for, among other things, equipment, supplies, training, personnel, and research and information systems for criminal justice efforts.

<sup>10</sup>In March 2009, the governor presented a proposed budget for fiscal year 2010 along with additional actions to again rebalance the fiscal year 2009 budget. Those actions included an additional reduction in the state's pension payment for fiscal year 2009, which allowed restoration of surplus in the current year which assisted in addressing a \$7 billion deficit for fiscal year 2010.

<sup>11</sup>New Jersey officials stated they are unable to estimate the total amount of Recovery Act funds that are coming into the state because some formula allocations have not yet been announced by federal agencies and some funding, such as increased FMAP funds, are subject to change based on future conditions.

Anticipating even less revenue in fiscal year 2010, which begins on July 1, 2009, the Governor has proposed a \$29.8 billion budget. According to the Governor, if New Jersey did nothing to curtail growth in state spending or adjust its mandatory obligations, the fiscal year 2010 budget would be about \$36 billion, or \$7 billion above anticipated revenues. In response to declining revenue, the Governor has proposed about \$4 billion in cuts to programs, rebates, pension payments, and state worker personnel costs. In all, more than 850 line items in the budget have been cut. The largest cuts will come from scaling back state rebates of local property taxes by \$500 million and reducing state payments to the pension fund by \$895 million. The Governor is also proposing to save \$400 million in personnel costs through a wage freeze and furloughs for state employees, avoiding an otherwise anticipated layoff of up to 7,000 state workers.

Some New Jersey officials began preparing for receipt of Recovery Act funds prior to passage of the Recovery Act. Anticipating federal stimulus spending for infrastructure, the Governor asked NJDOT to identify projects that could be ready for federal funding and quick implementation in November 2008. NJDOT officials identified about \$1.4 billion in potential eligible projects but had to scale this list back to meet New Jersey's eventual apportionment of Recovery Act transportation funds. The city of Newark also prepared a process with evaluative criteria for selecting local projects for Recovery Act funds before the Recovery Act was enacted.

New Jersey officials stated that New Jersey's plans for spending Recovery Act funds have been complicated by not having guidance from federal agencies immediately available and by preparations for the state's upcoming fiscal year 2010 budget. For example, the state Department of Education could not determine how the state could distribute its allocation of Recovery Act education funds until the U.S. Department of Education released its guidance on April 1, 2009. Officials from the state's Department of Community Affairs (DCA), which is responsible for housing and urban development programs in the state, stated that they lacked guidance from federal agencies for most of the programs that they administer, which hindered their preparation for use of those funds.<sup>12</sup> The Governor's Chief of Staff stated that some of the federal funds, especially the state's allocation of the SFSF funds, will be disbursed to the state in its

<sup>12</sup>DCA officials stated they did receive guidance from the U.S. Department of Energy on the weatherization program.

fiscal year 2010 budget, which is currently being debated by the state legislature.

New Jersey officials have been and are planning to continue submitting certifications for the state's use of Recovery Act funds. The Governor issued a certification memo to the Secretary of the U.S. Department of Transportation that the state would maintain its efforts with regard to state funding for the types of projects funded under the Recovery Act. Other local officials told us they would issue or had issued similar certifications for Recovery Act funds for which they are directly responsible. For example, NHA staff told us their Executive Director signed a certification letter for the Recovery Act funds that the NHA was responsible for.

**New Jersey Will Use Existing Resources for Recovery Act Oversight, but Lack of Additional State Funding May Hinder Its Efforts**

According to state officials, the Governor and executive branch agencies have primary responsibility for controlling the state's receipt of Recovery Act funds, with legislative approval.<sup>13</sup> To this end, the Governor has created the state Recovery Accountability Task Force, co-chaired by the Governor's Chief of Staff and the state's Comptroller and consisting of active and former state and federal officials. The task force will, among other things, monitor the distribution of Recovery Act funds in the state and promote the effective and efficient use of those funds. The task force has established a public Web site and will provide guidance for internal controls for complying with Recovery Act provisions. As part of the task force, the state Comptroller has responsibility for coordinating all of the oversight agencies in the state. These entities will have different roles in the state's Recovery Act oversight efforts:

- the state Auditor, who is appointed by the legislature and handles financial and some performance audits of state agencies;
- the state Comptroller, who is generally responsible for performance audits at the state and local levels of government and reviews government contracts over \$2 million;

<sup>13</sup>As described by state officials, similar to the federal government, each year the Governor submits to the legislature a proposed budget. The legislature has the ultimate authority to adopt the budget act and appropriate funds, subject to gubernatorial line-item veto. State agency use of federal funds must be authorized in state appropriations.

- the state Inspector General, who is responsible for investigations of fraud related to state government; and
- the internal audit offices that exist within most agencies, including the state Medicaid Inspector General and the contract compliance audit units within the Division of Purchase and Property (DPP) and the Division of Property Management and Construction (DPMC).

According to the state's Comptroller, the legislature's State Commission on Investigation, which is concerned with investigations on enforcement of state law, particularly regarding racketeering and organized crime, will also be among the agencies helping to ensure that the state's public employees who administer Recovery Act funds do so effectively and in compliance with federal or state requirements. In addition, the state legislature, state agencies, and many local entities (e.g., housing authorities, school districts, and metropolitan planning organizations) also have a role in overseeing these funds.

As described by state officials, Recovery Act funds must be used by state agencies pursuant to appropriation by the state legislature, and Recovery Act funds were appropriated in legislation enacted in March 2009. Under that legislation, the specific programs and activities conducted by those agencies with Recovery Act funds are also subject to approval by the legislature's Joint Budget Oversight Committee. However, according to state officials, any Recovery Act funds directly received by local governments or other entities in the state would not be budgeted or appropriated by the state legislature. State officials describe New Jersey as a strong "home rule" state and its constitution as giving localities many rights and responsibilities for providing local services. Therefore, New Jersey has more than 1,900 cities, counties, towns, townships, and local authorities or taxing districts, including 86 housing authorities, 566 municipal governments, and 616 school districts that can apply for, use, and potentially be held accountable for Recovery Act funds.

The Governor's Chief of Staff stated there is oversight of certain local activities at the state level. For example, state oversight of local public school districts has been enhanced in recent years in part through state

mandated limitations on compensation practices<sup>14</sup> and proficiency targets for state assessments have been raised. Additionally, the state has a significant amount of oversight over the three districts that are under state control to review and control their budgets. The U.S. Department of Education and the county superintendent have the authority to review these school districts budgets, as well. Further, according to the Governor's Chief of Staff, because the state already funds local school districts with \$8.8 billion in state funds, ensuring accountability for the use of state funds by school districts is not a new challenge to the state oversight agencies.

Many of the state and local agencies interviewed stated that their current accounting systems can track Recovery Act funds by program and project and can generate reports showing the use of those funds:

- Both the Newark and Trenton Housing Authorities stated that they use the Line of Credit Control System (LOCCS) accounting system, which HUD uses to provide funds to public housing authorities. LOCCS includes special accounting codes under which housing authorities can track Recovery Act funds by program and by type of use. Housing authorities can also use LOCCS to generate the required reports back to HUD showing how they have used Recovery Act funds.
- Both NJDOT and NJT stated that their accounting systems can track Recovery Act funds separately from their regular funds because they have created separate accounting codes to track these funds. Furthermore, most of the selected projects will be funded primarily with Recovery Act funds, making the process of tracking them easier.
- DPP officials stated that their current accounting system will be able to account for and control the use of Recovery Act funds used for procurement because DPP will create special accounting codes for these funds. These officials stated that their accounting systems had the capability to track funds using special accounting codes and that

<sup>14</sup>According to state officials, the state Department of Education has placed limitations on compensation and buyouts for high-level district administrators through a series of regulations and statutory changes. The Executive County Superintendent (a state employee) must review and approve, prior to district Board of Education approval, all employment contracts for the superintendent, deputy superintendent, assistant superintendent and business administrator, including new contracts, extensions, and renegotiations. There are specific state-imposed limitations on components of these contracts, like annuities, travel allowances, car allowances, and specific state limitations on buyout provisions in these contracts.

they were confident no special enhancements were needed to their accounting software, although they would monitor the accounting system to ensure it was functioning properly. DPP will also publicly advertise bids for projects funded with Recovery Act funds, include terms and conditions in each request for proposals and contract for these projects stating detailed reports required by the act, and will post contract award notices for Recovery Act funded projects.

- To track increased FMAP funds, New Jersey has established a discrete identifier in the state accounting system. The state has begun the process of adjusting systems, so that the additional FMAP funds can be tracked and monitored by specific service category. Despite these adjustments, tracking of these funds will not be dramatically different from how the state tracks funds for their overall budget. Additionally, the state is monitoring increased FMAP funds and comparing them against actual expenditures. According to New Jersey officials, the state is also monitoring unemployment levels to anticipate and project future FMAP levels.

New Jersey has not increased its number of state auditors or investigators, and there has not been an increase in funding specifically for Recovery Act oversight. Additionally, the state hiring freeze has not allowed many state agencies to increase their Recovery Act oversight efforts. For example, despite an increase of \$469 million in Recovery Act funds for state highway projects, no additional staff will be hired to help with those tasks or those directly associated with the act, such as reporting on the number of jobs that the Recovery Act funds created. While NJDOT has committed to shift resources to meet any expanded need for internal Recovery Act oversight, currently one person is responsible for reviewing contractor-reported payroll information for disadvantaged business enterprises, ensuring compliance with Davis-Bacon wage requirements, and job creation figures.

#### Potential Areas of Vulnerability of New Jersey Recovery Act Funds

In New Jersey's fiscal year 2007 Single Audit report, the independent auditor identified 42 significant control deficiencies related to compliance with internal controls requirements over major federal programs, 33 of which were considered to be material. Twenty-seven of the significant control deficiencies pertained to compliance with requirements for several major federal programs that the state administers—including Medicaid programs and Community Services Block Grants—through which the Recovery Act funds will flow. New Jersey has also faced challenges with internal controls with state entities in the recent past. For example, in

2005, the state Inspector General's review of the now-dissolved School Construction Corporation, which was responsible for more than \$8.66 billion in school construction funds, found the authority had "weak financial controls, glaring internal control deficiencies and lax or non-existent oversight and accountability" after it had disbursed \$4.3 billion in contracts and approved approximately \$540 million in changes to those contracts. In its place, in 2007, the state created a Schools Development Authority with a completely different management and accountability structure.

State officials noted that certain towns and cities, as well as regional planning organizations, can apply for and directly receive federal recovery funds under the terms of the Recovery Act. According to the state Inspector General, the risk for waste, fraud, and abuse increases the farther removed an organization is from state government controls. While some state officials said they have statewide investigative authority, they would not be able to readily track the funding going directly to local and regional government organizations and nonprofits as a result of the funding delivery and reporting requirements set up in the Recovery Act. In addition, staff from the state Auditor's office noted that some smaller cities and towns in New Jersey are not used to implementing guidance from the state or federal government on how they are using program funds, which could result in the localities reporting using funds for ineligible purposes. However, state Department of Education officials stated that although the sheer number of school districts in the state raises concerns, sufficient internal controls (state audits, Single Audits, state oversight, etc.) exist to prevent most instances of fraud and other illegal uses of funds.

As for state agencies, the Governor's Chief of Staff stated that the highest risk is associated with those agencies that will be responsible for managing significantly more money than ever before, compared with their normal budgets. While NJDOT officials stated they could accommodate about five times more Recovery Act funds than was received by New Jersey, other state officials stated that they were quickly developing plans to accommodate the influx of Recovery Act funds. For example, the Department of Community Affairs is responsible for implementing the state's allocation of \$118.6 million in Recovery Act weatherization funds, which is about double the normal amount. DCA officials stated that to avoid losing any of the state's allocation of weatherization funds, they were making contingency plans to redistribute any unused funds to other possible recipients under the weatherization program. According to the Governor's Chief of Staff, the state is trying to be rigorous about how these

programs are being designed and how they are using the funds. For example, state officials are emulating the federal oversight effort, in part by trying to build internal controls at the outset of the process and to use merit-based selection criteria for Recovery Act projects. The state Inspector General, in coordination with the New Jersey Recovery Accountability Task Force, will be conducting training at New Jersey government agencies concerning Recovery Act related internal control issues. As of April 17, the Inspector General hopes to present the first trainings by mid-May.

#### Plans to Assess Impact of Recovery Act Funds Are in Initial Stages and Vary across State and Local Agencies

The Governor's Chief of Staff stated that different state agencies are planning to evaluate the impact of Recovery Act funds. Assessing the impact of the increased FMAP funds will involve the extent to which the Medicaid program is able to accommodate additional applicants as a result of these funds. A New Jersey official noted that the state will have benchmark numbers on how many additional people are served and that this approach is no different from how the state would currently report impact. The state Auditor and the state Comptroller have also committed to carrying out audits and assessments of the impact of Recovery Act funds.

Officials we interviewed at New Jersey state agencies have different ways of either collecting or estimating data on the number of jobs created or retained as a result of Recovery Act funds. For example, the NHA will use payroll data to keep track of the exact number of union tradesmen and housing authority residents employed to turn damaged vacant units into rentable ones. In contrast, NJT is using an academic study that examined job creation from transportation investment to estimate the number of jobs created by contractors on its Recovery Act-funded construction projects.<sup>16</sup> Finally, officials stated that both DPP and DPMC both have methodology and mechanisms in place to track jobs created and maintained for goods and services procured under Recovery Act contracts.

<sup>16</sup>The study estimated that for every \$1 million of transportation infrastructure investment, 11 jobs are created, 70 percent of them are directly related to the investment, and 30 percent are indirectly related (Rutgers University Edward J. Bloustein School of Planning and Public Policy, "Economic Impacts of Planned Transportation Investments in New Jersey," New Brunswick, New Jersey, April 2008).



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**New Jersey's  
Comments on this  
Summary**

We provided the Governor of New Jersey with a draft of this appendix on April 17, 2009. The Governor's Chief of Staff responded for the Governor on April 20, 2009. In general, the Chief of Staff substantially agreed with the draft and provided technical comments that were incorporated, as appropriate.

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**Staff  
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In addition to the contacts names above, Raymond Sendejas, Assistant Director; Greg Hanna, analyst-in-charge; Jeremy Cox; Colin Fallon; Tarunkant Mithani; and Cheri Truett made major contributions to this report.

## Appendix XIV: New York

### Overview

**Use of funds:** An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation and education programs. The three largest funding categories are the Medicaid increased Federal Medical Assistance Percentage (FMAP) grant awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 13, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$3.14 billion in increased FMAP grant awards to New York.
  - As of April 13, 2009, New York had drawn down about \$1.74 billion, or 55 percent of its initial increased FMAP grant awards.
  - Nearly \$1.3 billion of the funds made available as a result of the increased FMAP were used to close the state's budget deficit for the fiscal year ending on March 31, 2009, or applied to lower the deficit for the current fiscal year. In addition, \$440 million was returned to the counties for their contributions towards the non-federal share of Medicaid expenditures that qualified for the increased FMAP.
- ✓ **Transportation—Highway Infrastructure Investment**
  - New York was apportioned about \$1.12 billion for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated about \$276.5 million for 108 projects to the New York State Department of Transportation. New York will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.
  - As of April 13, 2009, the New York State Department of Transportation had advertised for bids on 38 projects. Work on all of these projects is expected to begin this spring.
  - The state will target Recovery Act transportation funds to infrastructure rehabilitation, including preventive maintenance and reconstruction, such as bridge repairs and replacement, drainage improvements, repaving and roadway construction. State officials emphasized that these projects extend the life of infrastructure and can be contracted for and completed relatively easily in the 3-year time frame required by the act. Some Recovery Act funds will go to more typical "shovel-ready" highway construction projects for which there were insufficient funds.
  - By the end of April 2009, New York expects to have a complete list of transportation projects that Recovery Act funds will support.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - As of April 13, 2009, New York had been allocated about \$2.0 billion from the initial release of these funds by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that the states will meet maintenance-of-effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. As of April 13, 2009, New York had not submitted its application for these funds.
  - New York plans to use the majority of Fiscal Stabilization funding to support K-12 education costs for the 2009-2010 and 2010-2011 school years beginning July 1, 2009. New York education officials told us that most of the funds will be used to offset expected budget cuts throughout the school system that were caused by the downturn in the economy and in state revenues.

New York is also receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A, of the Elementary and Secondary Education Act (ESEA) (commonly known as No Child Left Behind), and the Individuals with Disabilities Education Act, Part B (IDEA). These are described throughout this appendix. Overall, New York expects to receive about \$26.5 billion in Recovery Act funds plus possible additional discretionary program funds over the next 3 years (fiscal years 2009-2011).

**Safeguarding and transparency:** New York plans to track and monitor Recovery Act funds mostly through its existing internal control, audit, and accounting systems, although the new Recovery Cabinet and other state institutions have initiated several steps to coordinate the oversight of Recovery Act projects. For example, the Office of the State Comptroller (OSC) is using its accounting system to tag and track these funds, while the New York State Department of Transportation (NYSDOT) is conducting a federal-aid risk assessment to focus its internal and contract audit resources on projects and contracts that may be most vulnerable to fraud, waste, and abuse. New York officials, however, expressed concerns about monitoring Recovery Act funds that do not pass through state offices but flow directly from federal agencies to local agencies or authorities. For example, the Metropolitan Transportation Authority, which provides transportation services for the New York City metropolitan area, expects to receive directly about \$1 billion in federal transit funds under the Recovery Act.

**Assessing the effects of spending:** Officials have taken some initial steps to meet the Recovery Act's reporting requirements, but generally they are awaiting further federal guidance. Officials throughout the state government expressed concerns about how to consistently report on the impact of Recovery Act funds.

### New York Beginning to Use Recovery Act Funds

New York has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance

Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup>

Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes. For the second quarter of fiscal year 2009, New York's FMAP was 58.78 percent, an increase of 8.78 percentage points over its fiscal year 2008 FMAP.

New York expects to receive about \$11 billion in federal Medicaid funds as a result of the increase in its FMAP. As of April 13, 2009, CMS had made about \$3.14 billion in increased FMAP grant awards to New York and the state had drawn down about \$1.74 billion of its grant awards. Nearly \$1.3 billion of the funds made available as a result of the increased FMAP was used to close the state's budget deficit for the state fiscal year ending on March 31, 2009, while \$440 million was returned to the counties for their contributions towards the non-federal share of Medicaid expenditures eligible for the increased FMAP.

New York initially plans to use funds made available as a result of the increased FMAP to help address budget deficits. According to the Governor's office, New York State has the highest Medicaid cost per capita and, unlike most states, requires local governmental entities to contribute

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

towards the nonfederal share of Medicaid expenditures. The state's counties provide this local share. According to state officials, in 2006, in order to control Medicaid spending at the local level, the state instituted a cap on local Medicaid expenditures that constituted about 33 percent of the nonfederal share of expenditures at the time. This cap, unique to New York, basically limits the annual increase in a locality's Medicaid expenditures to 3 percent of what it spent in 2005. The result has been that the localities' percentage share of Medicaid expenditures has slightly declined each year since 2006.

The 2009-2010 enacted state budget plans to use nearly half of the enhanced FMAP funding expected to be received through March 31, 2010 on (1) health care to avoid certain difficult provider reimbursement cuts, and (2) other savings actions proposed by the Governor in his initial budget proposal in December 2008. These funds will also help pay for unanticipated rising Medicaid costs, primarily driven by rising caseloads resulting from the current economic downturn. In addition, the FMAP funds (1) helped avoid proposed cuts to important human services and mental hygiene programs, (2) were used to maintain revenue sharing funding for New York City, and (3) avoided several proposed tax increases that would have impacted middle class families and small businesses.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing federal-aid highway Surface Transportation Program, through which money is apportioned to states for the construction and maintenance of eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds.

As of April 16, 2009, the Federal Highway Administration had obligated about \$276.5 million to New York State for 108 transportation projects.<sup>3</sup> The state has been able to move quickly on these projects largely because NYSDOT, as required by federal surface transportation legislation, has a planning mechanism that routinely identifies needed transportation projects and performs preconstruction activities, such as obtaining required environmental permits. A NYSDOT official told us that as of April 13, 2009, 38 projects approved in March 2009 had been advertised for bids for contracts.

In late 2008, NYSDOT began preparing to manage potential stimulus funding in transportation programs. NYSDOT, which oversees over 113,000 miles of highway, 16,000 bridges, and more than 130 transit operators, initially established a working group that began reviewing or “scrubbing” core projects in the state’s transportation improvement plan (STIP) in late 2008 to make sure projects would be fully permitted and “shovel ready,” should funding be made available. Because of an approximately 8 percent per year increase in construction costs during the last 3 years and the state’s declining fiscal position, New York has a large backlog of planned transportation projects. As of April 16, 2009, the Governor had certified that 108 projects met the objectives of the act and that the state will maintain its planned level of effort within its transportation program.

To meet the act’s objectives—funding projects that can be started quickly and have the desired economic impact in terms of jobs and local benefits—the state will target most state transportation funds to infrastructure rehabilitation, including preventive maintenance and reconstruction, such as bridge repairs and replacement, drainage improvement, repaving, and roadway reconstruction. State officials emphasized that these projects extend the life of infrastructure and can be contracted for and completed relatively easily in the 3-year time frame required by the act. The state will also target some Recovery Act highway dollars to more typical “shovel ready” highway construction projects for which there are insufficient funds. By the end of April 2009, NYSDOT expects to have a complete list of projects that Recovery Act funds will

<sup>3</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government’s contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

support. NYSDOT officials noted that the list of projects would be fluid depending on bid results, budget overruns, and the ability of localities to start and complete planned projects within expected time frames.

Consistent with the Governor's goal of leveraging the impact of Recovery Act funds, NYSDOT has also begun working with rural public transportation systems to identify eligible Federal Transit Administration activities. Recovery Act transit funds will be used to replace a significant number of vehicles that currently exceed their federally rated service life with new cleaner-fuel buses that comply with the Americans with Disabilities Act. NYSDOT will use a statewide bus contract to procure the majority of these new vehicles. This cooperative effort would also allow the communities to take advantage of the state's procurement expertise and presumably lower overall procurement costs.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). SFSF is intended to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers. As of April 13, 2009, New York's SFSF allocation was about \$2.0 billion; however, the state had not drawn down any of this amount. The state has not applied for these funds and they will not be allocated to public entities such as K-12 school districts and public higher education institutions until the school year begins on July 1, 2009. The Governor's office said that this application is expected to be submitted soon.

The New York State Education Department (NYSED), which has an annual budget of about \$30 billion, expects to receive about \$5 billion in Recovery Act funds. About half of the amount—approximately \$2.5 billion—is expected to be provided through SFSF. These funds can be used to help avert elementary, secondary, and higher education reductions, such as the loss of teachers. NYSED officials told us that they believe most of these funds will be used to offset expected budget cuts throughout school systems that were caused by the downturn in the economy and in state revenues. State officials also have discretion over an additional 18 percent of the stabilization funds—approximately \$549 million—and can use this portion for a wide range of government services, including school modernization.

As of April 13, 2009, New York had also been allocated an additional \$1.7 billion in Recovery Act funds for programs under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA), as amended by the No Child Left Behind Act, and the Individuals with Disabilities Education Act (IDEA).

#### **New York Has Established a Recovery Cabinet to Manage Recovery Act Funds**

The key New York institutions involved in managing Recovery Act funds are the governor's office, the state program departments and agencies, and OSC. In addition, localities, transit, or housing authorities will play a role in managing some Recovery Act funds that do not pass through state offices. Because of the timing of New York's annual fiscal year and the February 17, 2009, enactment of the Recovery Act, the state had to quickly incorporate Recovery Act funding into the budget for the fiscal year beginning April 1, 2009. New York's Governor, in anticipation of the Recovery Act, established a Recovery Cabinet in February 2009. The Recovery Cabinet is led by the Governor's Senior Advisor for Transportation and Infrastructure. All state agencies and many state authorities are represented on the cabinet, which is charged with coordinating and managing Recovery Act funding throughout the state. Similarly, New York City officials developed a City Hall Working Group comprising city management and individuals from the relevant agencies that are planning to receive Recovery Act funding to coordinate and manage the funding.

While over 50 percent of Recovery Act funding, such as most education program funding, is formula driven and directed to specific localities in the state, other funds may be allocated by the state, such as discretionary funds for rail projects. A Recovery Cabinet committee is making such funding decisions in a "situation room" that works with the relevant state departments to disburse recovery funds in a manner that seeks to maximize the act's objectives and address the political need to spread money throughout the state. More specifically, the cabinet expects to leverage Recovery Act funding in transportation and other areas to maximize the economic impact of the funds. The cabinet also established other working groups to address communication and coordination objectives, including one group that is working on Recovery Act reporting requirements. State officials expressed concerns about the Recovery Act's requirements for reporting 10 days after the quarter ends. The officials said that this is a potential area of noncompliance for New York, particularly because the state does not have a strong track record on reporting compliance. Furthermore, state officials expressed concerns about how



Recovery Act administrative and monitoring costs might strain existing financial and human resources.

The Recovery Cabinet also serves as a focal point of contact for counties and other localities throughout the state—informing them of the types of projects that could be eligible for stimulus funding and soliciting ideas and proposals for such funding. In addition, New York established an economic recovery Web site in February 2009—[www.recovery.ny.gov](http://www.recovery.ny.gov). By using the Web site, New Yorkers have been able to enter their project ideas directly into a project database and track Recovery Act funding and its impact. This database currently contains over 16,000 project ideas.

Other key players in New York's management of Recovery Act funds include OSC, an independently elected office that is charged with issuing the state's internal control standards, managing the central accounting system, and directing internal audits throughout the state's departments and agencies, among other responsibilities. OSC will be responsible for tracking and monitoring the progress of Recovery Act funding and ensuring that the funding meets established internal controls.

State authorities and metropolitan planning organizations that are not directly managed by the Governor are also key players in the delivery of New York State services and are therefore central to the management of some Recovery Act funds. For example, the Metropolitan Transportation Authority will manage about \$1 billion of Recovery Act funds.

### **New York Plans to Oversee and Safeguard Recovery Act Funds Using Existing Control Mechanisms Where Possible**

The primary responsibility for ensuring the transparency and accountability of Recovery Act funds rests with the executive branch, led by the governor. For the most part, New York plans to track and monitor Recovery Act funding using existing internal control, audit, and accounting systems. For example, OSC plans to use its existing Central Accounting System to tag and track Recovery Act funds as they are disbursed. Individual state agencies are also planning to use their existing management systems to monitor Recovery Act spending. For example, NYSDOT is conducting a federal-aid risk assessment to help its Internal Audit and Contract Audit Bureaus target their resources to the most vulnerable programs and projects. However, state officials have several oversight concerns, including monitoring Recovery Act funds that do not pass through state agencies and the ability of some local authorities that may not have experience managing federal programs to oversee large infusions of new funding. Finally, many officials throughout the state are

concerned about their ability to consistently report on the impact of Recovery Act funding.

#### New York Will Use Existing Control Structure

Several New York government entities are responsible for the management, implementation, and oversight of internal controls and for safeguarding taxpayers' money. These entities include OSC, individual state agencies, and the governor's office. For example,

- OSC is responsible for the state's Central Accounting System, disburses funds, and audits state agencies and authorities, among other responsibilities.
- Each large state agency, such as NYSDOT, has a director of internal audit,<sup>4</sup> as well as an internal control officer<sup>5</sup> who reports to the head of the agency, coordinates internal control activities, and helps ensure internal control program compliance.
- The head of each state agency and public authority must annually certify compliance with the State's Internal Control Act.
- Each state agency operates its own financial management and reporting system and has its own procurement officer. However, OSC must review and approve all contracts over \$50,000.

The governor's office, in addition to overseeing state agencies, is responsible for conducting an annual audit of federal funds known as the Single Audit. New York's Single Audit for the year ending March 31, 2008, disclosed a number of material weaknesses involving the major federal programs. For example, the Single Audit found the following:

- OSC's procedures, through which OSC identified approximately \$49.8 million in potential overpaid Medicaid claims, were adequate. The Department of Health and the Office of the Medicaid Inspector General have initiated recovery of those claims that they determined are

<sup>4</sup>The agency's director of internal audit reviews the operations of the agency to provide reasonable assurance of conformance with management policies and the effectiveness of internal controls. The internal auditor must maintain independence from the activities that are audited.

<sup>5</sup>The internal control officer assists the agency head and agency management and has responsibility for implementing, maintaining, and reviewing the agency's system of internal control.

appropriate for recovery. OSC had also identified about \$17 million in potential overpaid claims in 2007. State officials told us, however, that many of the instances of potential Medicaid overpayments were without basis and were, in fact, made consistent with federal requirements.

- NYSDOT did not adequately document audit extensions that it granted subrecipients. Furthermore, the department did not have a sanction policy in effect for subrecipients that were not in compliance with audit requirements. Effective August 2008, NYSDOT established a formal sanctioning policy.
- The Housing Trust Fund Corporation did not have procedures in place to adequately monitor the compliance requirements of the Single Audit Act, as amended, and OMB's implementing guidance in OMB Circular No. A-133, for grant subrecipients.
- Several programs, including Temporary Assistance for Needy Families, the Child Care and Development Block Grant, and the Office of Children and Family Services, did not adequately complete forms documenting the transfer of funds awarded by the federal government.
- The Department of Education's Vocational Rehabilitation Services program had not determined individuals' eligibility for the program services within a reasonable period of time.

The Single Audit did not provide 10 federal programs, including the Medical Assistance, Low-Income Home Energy Assistance, and Food Stamp Cluster Programs, an unqualified opinion because of various findings, including cost allocation plans that were not approved by the federal government. New York also received an unqualified opinion on OSC's comprehensive annual financial statements for the state fiscal year that ended March 31, 2008.<sup>6</sup> The audit reported control deficiencies but disclosed no instances of noncompliance that would be material to the basic financial statements.

As noted above, the state will separately account for Recovery Act expenditures on the Central Accounting System to make tracking the funds easier. However, according to a state comptroller official, agencies

<sup>6</sup>For an unqualified opinion, the auditor expresses the opinion that the financial statements present fairly, in all material respects, the financial position, results of operations, and cash flows of the entity in conformity with generally accepted accounting principles.

may rely on multiple databases for handling transactional and performance data, making data reliability difficult to ascertain. According to this official, state agencies vary in their capabilities, and the independent financial management systems that operate distinctly from the Central Accounting System have varying degrees of sophistication and accessibility.

**The Governor Plans to Implement Several Internal Control Initiatives for Recovery Act Funding**

In addition to existing control systems, the Governor's office has planned several new initiatives for ensuring accountability of Recovery Act funds. First, drawing on past efforts of New York state agencies and the New York State Internal Control Association to improve the state's internal controls, transparency, and data integrity, the Recovery Cabinet plans to establish a working group on internal controls. This working group will be made up of internal control officers from major agencies in the cabinet and will meet regularly to provide additional guidance to those agencies receiving and or administering Recovery Act funds. Second, the Governor's office plans to hire a consultant to review the state's management infrastructure and capabilities to achieve accountability, effective internal controls, compliance, and reliable reporting under the Recovery Act. Third, the Director of State Operations provided initial guidance to the state agencies and authorities on the Recovery Act accountability and transparency requirements. According to state officials, all agencies and departments that expect to receive Recovery Act funds have been asked to review and report on their practices for fraud prevention, contract management, and grants accountability to assess their current vulnerabilities and to ensure that the state is prepared to meet the Recovery Act requirements. Finally, the state plans to coordinate fraud prevention training sessions.

**Office of the State Comptroller Issued Guidance for Safeguarding Recovery Act Funds**

On March 23, 2009, OSC issued accounting bulletins and procurement and disbursement guidelines to state agencies on using Recovery Act funds. Included in these guidelines are instructions to agencies on using a designated revenue code to account for all federal grant moneys received and a designated accounting code to process and report payments financed with Recovery Act funds. According to OSC, it intends to closely scrutinize contracts and monitor payments charged to Recovery Act appropriations to ensure adequate accountability, compliance, and effective and efficient use of Recovery Act funds. In addition, OSC says it plans to post the Recovery Act data that will flow through the central accounting system to Open Book, the Web site that provides transparency for contracts, expenditures, and local government funds. Furthermore,

OSC says that it will continue to advise and provide technical assistance to local governments as the requirements of the Recovery Act become clearer.

#### Examples of State Agencies' Planned Oversight and Reporting of Recovery Act Funds

Guided by the Recovery Cabinet working groups, state agencies are planning to implement various types of oversight and reporting mechanisms to comply with the Recovery Act. For example:

- NYSDOT is relying heavily on existing program oversight controls, such as normal highway project procurement requirements, to manage and control Recovery Act spending. In addition to those oversight controls, as described above, NYSDOT is conducting a risk assessment of federal-aid projects to direct future internal audit and contract reviews. NYSDOT officials said that special emphasis will be placed on high-risk areas, such as projects developed by local public agencies, and that a formal plan for overseeing Recovery Act subrecipients will include training, technical assistance, and regular reviews of subrecipients' documents and processes. With regard to reporting, NYSDOT is developing a dataset that is expected to contain all data elements required to fully meet state reporting requirements. NYSDOT is also putting a reporting requirement in existing recovery project contracts alerting contractors that they are responsible for meeting all Recovery Act reporting requirements.
- NYSED officials said that they have been meeting with OSC to ensure proper accounting codes are used in tracking and reporting Recovery Act funds. However, officials are concerned that once the funds reach localities, the funds may lose their accounting codes and get rolled up with other state and federal funds. In addition, state education officials said that they have established a waste, fraud, and abuse work team to examine risks and identify areas of concern associated with Recovery Act funds. The officials said that the biggest challenge that they foresee is district reporting at the school level. According to the officials, risk assessments for schools with higher spending per student will need to be developed.
- Division of Housing and Community Renewal officials said that they are fairly confident that they can modify the division's existing accounting and reporting systems to meet Recovery Act requirements. However, housing officials are concerned about the potential for fraud, waste, and abuse in the weatherization program. This concern results from the huge increase (over 600 percent) in funding New York will get, rule changes, the acceleration of the expenditure time line, and the

need to hire subcontractors, many of which will be new to the program. Specifically, New York State expects to receive \$395 million in additional weatherization funds from the Recovery Act, compared with a little over \$60 million allocated to the program in the previous state fiscal year. In addition, the Recovery Act increased the maximum amount that can be spent for each housing unit qualifying for the program from \$2,500 to \$6,500. Officials said they are concerned about their ability to effectively manage the program, given the major funding and program changes caused by the Recovery Act, when their existing staff is already stretched. Housing officials said that they are assessing the risk to the weatherization program.

- According to New York officials, increased FMAP grant awards are segregated from other Medicaid funds received by the state. These funds have received a distinct code to identify them as part of the funding received from the Recovery Act in OSC's Central Accounting System. Additionally, the increased FMAP grant awards received by the state and local governments are tracked separately in the accounting system. OSC has instructed localities to maintain a separate account for FMAP funds. As of April 13, 2009, the comptroller had not disclosed plans for auditing the increased FMAP funds.

#### Plans to Assess Impact Are Still Being Developed

State transportation, education, and housing agency officials are just beginning to consider plans to assess the impact of Recovery Act funds. They are generally waiting for the Office of Management and Budget to provide guidance or methods to help in assessing impact, such as job retention and creation, increases in tax revenues, and savings from weatherization or other energy projects. For instance, state housing officials said that they typically track dollars and that they will require additional guidance from the Department of Housing and Urban Development on how to track job creation. State education officials said that it would be difficult to isolate the impact of Recovery Act funds on student achievement from the impact of other initiatives the state is undertaking. State officials also expressed concerns about how to consistently measure the impact of funding, such as how to count job creation and how to track the ripple effect of funding.

New York City officials said that it will be a challenge, absent additional guidance, to account for the impact of Recovery Act funds on programs funded by multiple streams of money, such as counting the number of new beds at a homeless shelter or the number of additional children in the city's child care program. New York City is developing an online database that will describe the use of Recovery Act funds down to the program

## Appendix XIV: New York

level. Officials said that the purpose of the database is to provide transparency for New York City residents and to fulfill future reporting requirements. The database is expected to provide such details on a Recovery Act-funded program as the number of additional beds at a homeless shelter. However, New York City officials said that it is difficult to begin planning how to assess impact until they know what measures will be called for by federal reporting guidelines. Furthermore, New York City officials recommended relaxing the reporting deadlines and requirements for the first quarter after Recovery Act funds are received so states and localities have more time to understand new guidance.

#### New York's Comments on This Summary

We provided the Governor of New York with a draft of this appendix on April 17, 2009. The Senior Advisor for Transportation and Infrastructure responded for the Governor on April 20, 2009 by providing technical suggestions that were incorporated, as appropriate.

#### GAO Contacts

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#### Staff Acknowledgments

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## Appendix XV: North Carolina

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, Centers for Medicare & Medicaid Services (CMS) had made about \$657 million in increased FMAP grant awards to North Carolina.
  - As of April 1, 2009, North Carolina had drawn down \$414.6 million in increased FMAP grant awards, or 63 percent of its awards to date.
  - North Carolina officials reported that they plan to use funds made available as a result of the increased FMAP to maintain current populations and benefits and to offset the state's general fund deficit.
- ✓ **Transportation—Highway Infrastructure Investment**
  - North Carolina was apportioned about \$736 million for infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated about \$165 million for 53 projects in North Carolina.
  - As of April 16, 2009 the North Carolina Department of Transportation had selected 138 projects estimated to utilize about 90 percent of its allocated Recovery Act funds.
  - These projects include activities such as repaving highways and replacing bridges.
  - North Carolina Department of Transportation officials told us they identified these projects based on Recovery Act criteria that priority is to be given to projects that are anticipated for completion within a 3-year time frame and that are located in economically distressed areas.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - North Carolina was allocated about \$952 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. North Carolina officials said that they would apply for fiscal stabilization funds by the end of April 2009.
  - The state had not yet determined how fiscal stabilization funds will be used.



North Carolina is also receiving additional Recovery Act funds under other programs, such as Edward Byrne Memorial Justice Assistance Grant program to improve the functioning of the criminal justice system; the Tax Credit Assistance Program for low-income housing; and Workforce Investment Act Youth, Adult, and Dislocated Worker Programs that provide employment and training services. The status of state plans for using these funds is described throughout this appendix.

**Safeguarding and transparency:** The state has set up the Office of Economic Recovery and Investment (OERI) to help agencies track, monitor, and report on Recovery Act funds, and the North Carolina Senate and House of Representatives have established committees to provide legislative oversight of these funds. In addition, the state has a number of initiatives under way that will improve accountability and transparency for Recovery Act funds, and the state will track Recovery Act funds separately to ensure accountability for those funds. North Carolina officials identified several potential concerns about the safeguarding of funds. For example, several officials said that they were concerned about whether there were enough staff members to meet additional management and oversight responsibilities under the Recovery Act.

**Assessing the effects of spending:** North Carolina agencies are in the early stages of developing plans to assess the impact of Recovery Act expenditures. According to state officials, they have been awaiting guidance from the federal government, particularly related to measuring job creation.

### North Carolina Beginning to Use Recovery Act Funds

North Carolina has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008,

and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs, (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs, and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act are for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, North Carolina had drawn down \$414.6 million in increased FMAP grant awards, or 63 percent of its awards to date.<sup>3</sup> North Carolina officials reported that they plan to use funds made available as a result of the increased FMAP to maintain current populations and benefits and to offset the state's general fund deficit. The state has received guidance on the requirements for reporting Medicaid expenditures under the Recovery Act. However, the state would like additional guidance on other types of reporting requirements, such as performance information.

**Transportation – Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary

<sup>1</sup>Recovery Act, div. B, Title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

<sup>3</sup>North Carolina received increased FMAP grant award of \$657.1 million for the first three quarters of federal fiscal year 2009.

legal reviews and determined that the projects are an appropriate use of taxpayer funds. North Carolina provided these certifications, but conditioned the level of funding from state sources for the Recovery Act covered programs on future revenue collections in the state.<sup>4</sup>

The North Carolina Department of Transportation (NCDOT) was apportioned about \$736 million in Recovery Act funds for highways and bridges. As of April 16, 2009, the U.S. Department of Transportation had obligated about \$165 million for 53 projects in North Carolina.<sup>5</sup> The department has plans to award 70 contracts for Recovery Act projects between March and June, which are estimated to cost \$466 million. NCDOT officials told us that they identified these projects based on Recovery Act direction that priority is to be given to projects that are anticipated to be completed within a 3-year time frame and that are located in economically distressed areas. Projects were also evaluated based on several criteria, including alignment with long-range investment plans and considerations about geographical diversity and economic impact.<sup>6</sup> Based on the estimated costs of the initially selected projects, about one-third of costs are for projects not located in economically distressed areas, according to state officials.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures it will take action to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly

<sup>4</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the Department of Transportation and has not been reviewed by GAO.

<sup>5</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

<sup>6</sup>Projects selected were evaluated based on several other criteria, including a state equity formula (North Carolina G.S. 136-17.2A) that creates a target value for programming future expenditures in various regions of the state. The formula is applied only to non-exempt highways funds and not transit and rail programs.

qualified teachers. North Carolina officials said that they would apply for fiscal stabilization funds by the end of April 2009.

The state has been allocated \$952 million under the SFSF program. Officials from the state education agency, the North Carolina Department of Public Instruction, said that 81.8 percent of the SFSF would be distributed to school districts and institutions of higher education in accordance with Recovery Act requirements. State officials are in the process of determining how to calculate the relative amount of funding that school districts and public institutions of higher education would receive. Regarding the other 18.2 percent of SFSF, state officials said that a decision had not yet been made about how these funds would be allocated. State officials have emphasized in their communications with school districts that funds should be used for short-term investments with potential for long-term programmatic gains, echoing federal guidance.

**U.S. Department of Justice Edward Byrne Memorial Justice Assistance Grant Program:** The Edward Byrne Memorial Justice Assistance Grant Program (Byrne Grant Program) was established to streamline justice funding and grant administration, and allows states, tribes, and local governments to support a broad range of activities to prevent and control crime based on their own local needs and conditions. According to officials of the North Carolina Governor's Crime Commission, the office expects to receive an allocation of \$34.5 million through the Byrne Grant Program. The Governor's Crime Commission is allowed to use 10 percent of that total, or about \$3.5 million, for administrative purposes. This leaves a balance of \$31 million. Of this amount, 42.4 percent, or \$13.2 million, must be passed through by formula to local governments and the remainder of \$17.9 million will go to other state agencies and institutions. North Carolina officials for the Byrne Grant Program are planning to fund programs based on the state's list of program priorities, which include programs such as the Criminal Justice System Improvement, Crime Victims' Services, Juvenile Justice Planning, and North Carolina Gang Prevention Initiative. Also, the localities within the state will receive \$21.9 million, which will be awarded by the U.S. Department of Justice.

**Tax Credit Assistance Program and the Low Income Housing Tax Credit (LIHTC) Exchange Program:** The Tax Credit Assistance Program provides grant funding for capital investment in Low Income Housing Tax Credit (LIHTC) projects using a formula-based allocation to state housing credit allocation agencies. The LIHTC Exchange program provides grants for housing projects in lieu of LIHTC allocations. The

housing credit agencies in each state distribute these funds competitively and according to their qualified allocation plan. According to officials with the North Carolina Housing Finance Agency (NCHFA), the state has identified potential projects for the Tax Credit Assistance Program (TCAP), focusing initially on 40 to 50 tax credit projects that were stalled due to a lack of financing from other sources. NCHFA officials said they are waiting on guidance from the U.S. Department of Housing and Urban Development and Department of the Treasury before they begin the application process for developers. NCHFA officials said that environmental review requirements could pose a challenge to meeting federal timelines for making awards, but that they would not know for certain until final federal guidance has been issued.

**Workforce Investment Act Youth, Adult, and Dislocated Worker Programs:** The Workforce Investment Act (WIA) provides funds for employment and training services to youth, adults, and dislocated workers. North Carolina was allocated nearly \$80 million through these WIA programs under the Recovery Act. The North Carolina Department of Commerce (DOC) has been working with local workforce development boards since January to help them plan and prioritize the use of these Recovery Act funds. The state has communicated these priorities to the local workforce development boards: (1) increasing the number of people served and trained, (2) targeting programs toward underserved populations, including those receiving public assistance, (3) implementing a statewide summer youth employment program, and (4) increasing support services, such as child care and transportation. As necessary, the department has worked with other state departments to coordinate efforts. For example, DOC has coordinated with the state community college system to create short-term course offerings in 12 high-growth occupations that lead to certificates at each of the 58 state community colleges. DOC officials are also developing plans to use state-level funds received under the Recovery Act, and anticipate using those funds to help conduct outreach to inform the public of available programs and services funded through the Recovery Act.

#### Background Information on North Carolina

Federal funding plays an important role in North Carolina's state budget, with the state receiving a total of about \$12 billion for fiscal years 2007-2008, which accounted for about one-quarter of the total state budget of about \$41 billion. Health and Human services, at about \$16 billion, and education, at about \$15 billion, were the two largest categories of state spending, together accounting for more than 70 percent of the state budget. Federal funds accounted for more than half of total state spending

on health and human services, and about 10 percent of state spending on education.

North Carolina is expecting to receive an estimated \$6.1 billion of the Recovery Act funding going to states. North Carolina's fiscal situation is not unlike many other states. In the midst of its economic crisis, the Governor's proposed biennial budget contains \$2.6 billion in spending reductions and \$1.3 billion in revenue increases, and proposes to use \$2.9 billion of federal recovery funds to support education and other mission-critical services over the biennium. The Governor's budget proposal indicated that most programs face reduced or level funding, but recommended continued focus on growing North Carolina's economy, improving public education, keeping higher education accessible and affordable, and protecting the state's most vulnerable citizens.

North Carolina, after 3 consecutive years of growth, suffered a significant economic decline in 2008. As reported in the Governor's budget proposal, the state lost over 120,000 jobs—a nearly 3 percent decline—in 2008, pushing its unemployment rate up to about 10 percent. Job losses were particularly steep in the manufacturing sector, but the state reported that its housing sector, while also suffering a decline, was less affected by the housing downturn than other states. The Governor's budget proposal projects the economy to continue its decline, but to stabilize in 2010 and begin to grow in 2011. In general, the state projects economic performance to outpace the U.S. average.

The North Carolina state government operates on a biennial budget cycle, which begins on July 1 of odd-numbered years. The North Carolina constitution requires the Governor to submit a balanced budget, and state statute requires the General Assembly to pass a balanced budget, according to the National Association of State Budget Officers. North Carolina's General Assembly must pass an appropriations bill in order for state agencies to disburse federal funds, according to state officials, according to NASBO.

North Carolina's Governor, Beverly Perdue, took office in January of 2009. The Governor is supported by a 10-person cabinet that she appoints, and in February 2009, she established the Office of Economic Recovery and Investment (OERI) to oversee the state's implementation of the Recovery Act. Several other key state-level executive positions, including the

Treasurer and the Superintendent of Public Instruction,<sup>7</sup> are selected through statewide elections. Also, the State Auditor, who is responsible for providing independent evaluations and audits of state agencies and programs, is selected by statewide election. North Carolina has a bicameral General Assembly, with members of both the House and Senate being elected to 2-year terms. The General Assembly typically meets for a full session in odd-numbered years and a shorter session in even-numbered years. There is no concluding date for either session, according to state officials.

**North Carolina's Planning Process Is Being Led by the Newly Created Office of Economic Recovery and Investment**

On February 17, 2009—the same day the Recovery Act was enacted—Governor Perdue created the OERI to oversee North Carolina's handling of federal stimulus funds as well as state-level economic recovery initiatives. OERI's responsibilities include, among other things, coordinating state efforts to track and report on Recovery Act funds and maximizing the state's use of Recovery Act funds. Another of OERI's major responsibilities is to provide guidance to state departments and localities on how to monitor, track, and report the use of Recovery Act funds. On March 30, 2009, the state issued a memorandum on budgeting and accounting for Recovery Act funds. This memorandum is the first of what is anticipated to be a continuing series of information and directives to ensure that state agencies and subrecipients comply with federal and state requirements. Specifically, this memorandum provides guidance requiring that Recovery Act funds may not be commingled with other funds and that Recovery Act expenditures will require review and approval by the Office of State Budget and Management (OSBM). In addition, OERI has established two management directives requiring agencies to make weekly reports on Recovery Act funds, and to submit grant applications to OERI for review.

Also, OERI is creating several working groups to coordinate state implementation of Recovery Act programs and requirements. Specifically, working groups from OERI and OSBM are being established for each recipient agency and grant program to ensure close coordination, clear establishment of operating procedures, and improved communications. According to OERI's Director, three working groups for education, housing and homelessness, and health information technology, have been established, and more are planned. OERI has also developed a senior state

<sup>7</sup>The Chief Executive Officer of the State Board of Education is appointed by the Governor.

management team with representatives from state agencies to exchange information and facilitate Recovery Act implementation.

Governor Perdue's budget proposal, which according to state documents incorporated an anticipated \$6.1 billion in Recovery Act formula funds, is currently being considered and reviewed by the General Assembly. In an effort to monitor and oversee these Recovery Act funds, the North Carolina Senate established the Select Committee on Economic Recovery. According to the committee's Chairman, the new committee was established to have legislative review of how the Recovery Act funds will be used and the effect the funds may have on the state's budget. The North Carolina House of Representatives has established a similar committee.

#### Plans for Safeguards and Controls Being Developed at the State Level and at State Agencies Administering Federal Programs

As North Carolina prepares for the receipt, tracking, monitoring, and reporting of Recovery Act funds, it currently faces a number of known financial management challenges and other risks. For example, North Carolina's 2007 Single Audit report had 18 findings for material weaknesses and material noncompliance related to issues with federal program compliance for the North Carolina Departments of Health and Human Services (16) and Crime Control and Public Safety (2). Five of the 18 findings were related to insufficient subrecipient monitoring. The state auditor's office also noted that single audit findings have consistently found issues related to subrecipient monitoring by state agencies. Insufficient subrecipient monitoring and other deficiencies such as these may leave Recovery Act funds vulnerable to fraud, waste, and abuse.

In addition to single audit findings, some state officials identified challenges for state agencies responsible for overseeing Recovery Act funds. For example, several state officials said they were concerned about the adequacy of staff and funds needed to meet additional management and oversight responsibilities under the Recovery Act. In particular, officials with the Department of Public Instruction noted that it would be difficult to add staff to take on anticipated additional monitoring and reporting requirements. State officials told us they will explore the possibility of receiving a waiver from the U.S. Department of Education that would allow the state to set aside additional Recovery Act funds under Title I, Part A of the Elementary and Secondary Education Act of



1965 (ESEA, commonly known as No Child Left Behind).<sup>8</sup> However, officials in other agencies, such as the North Carolina Department of Commerce, which administers Workforce Investment Act funds, felt that they would be able to absorb additional responsibilities with current staff and resources. State officials also identified programs that were receiving a significant increase in program funding as a risk. For example, several officials noted that the weatherization program is receiving a substantial increase in funding. Finally, state officials told us that state agency guidance and communications with local governments are areas that will bear watching, as ensuring that local governments understand how to properly account for and segregate federal and state funds will be critical.

#### Plans for Oversight of North Carolina's Recovery Act Funds

Within the state of North Carolina, a variety of efforts are under way to establish new safeguards over Recovery Act funds, including some that will build on current systems and recent initiatives. For example, officials at North Carolina's OSC and OSBM told us that several state agency accounting systems will need to be modified to track Recovery Act funds as required by the Recovery Act. OSBM officials told us that they have been waiting for Office of Management and Budget (OMB) guidance on the reporting requirements, which was released by OMB on April 3, 2009. These officials have not identified any state agency accounting systems that are incapable of adding a unique identifier code to separately track Recovery Act funds, but said that nearly all systems will need some modifications. A bigger concern is that Recovery Act reporting time frames may not be aligned to the state departments' normal accounting cycles, which may delay the departments' ability to provide monthly or quarterly reports to OSBM and OERI.

North Carolina officials also told us that they plan to build on recent statewide transparency and accountability initiatives to help meet reporting and oversight requirements. For example, the state plans to use its Web site, [www.NCOpenBook.gov](http://www.NCOpenBook.gov), to include information on contracts and grants awarded with Recovery Act funds. In addition, North Carolina has created another Web site, [www.NCRecovery.gov](http://www.NCRecovery.gov), designed to maintain a record of how Recovery Act funds are being spent in a way that is transparent and accountable. Although still under development, plans for

<sup>8</sup>In ESEA Title I guidance released by the Department of Education on April 1, 2009, the department noted that it would propose regulations adjusting state administrative expenditure caps in order to help states defray the costs of data collection requirements in the Recovery Act.

this Web site include the ability to provide additional information about how funds will be distributed, information on how to apply for funds or contracts, a mechanism to track spending on individual projects, and estimates of the economic impact and jobs created. Additionally, OSBM, in consultation with the state Department of Administration, Division of Purchase and Contract, is reviewing a statewide procurement process to streamline the process and identify any areas that need to be improved. The results of this review may indicate either systemic statewide or individual agency needs related to the Recovery Act. Finally, the OSC is phasing in a statewide internal control program called EAGLE (Enhancing Accountability in Government through Leadership and Education), which is intended to establish adequate internal controls and increase fiscal accountability. Under the EAGLE program, each agency will be required to perform an annual assessment of internal controls over financial reporting and identify risks.

North Carolina's State Auditor told us that, given current staffing levels, her office will conduct as many oversight reviews and audits of Recovery Act funds as they can. In order to handle the new Recovery Act work, it will be necessary to cut back on some of the other fiscal control audits. The State Auditor told us that she uses a risk-based approach to auditing and plans to focus the State Auditor's Recovery Act work on subrecipient monitoring and on how the Recovery Act funds are being segregated from other federal funds coming through traditional funding streams. The State Auditor's office also noted that OMB and other federal agency guidance may identify areas that may merit closer scrutiny.

### Plans to Assess Impact of Recovery Act Funds Are Just Being Developed

State officials across agencies told us that that the state Office of Economic Recovery and Investment was developing guidance on the Recovery Act reporting requirements, but that the state has not yet begun assessing the effects of Recovery Act funds. The state provided localities with guidance on a number of Recovery Act-related topics on March 30, 2009, but the guidance has not yet specifically addressed Recovery Act reporting requirements. State officials told us that they needed federal guidance about how to assess the effects of Recovery Act funds before they can release state guidance. For example, the state's Chief Procurement Officer said that the state needs guidance about how to measure specific reporting requirements such as jobs created and jobs saved.

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**North Carolina's  
Comments on This  
Summary**

We provided the Governor of North Carolina with a draft of this appendix on April 17, 2009. The Director of OERI responded for the Governor on April 20, 2009. In general, the comments were either technical or were status updates. The official also provided technical suggestions that were incorporated, as appropriate.

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In addition to the contacts named above, Bryon Gordon, Assistant Director; Scott Spicer, analyst-in-charge; Carleen Bennett; George Depaoli; Bonnie Derby; Leslie Locke; Stephanie Moriarty; and Anthony Patterson made major contributions to this report.

## Appendix XVI: Ohio

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made about \$760 million in increased FMAP grant awards to Ohio.
  - As of April 1, 2009, Ohio has drawn down about \$420.6 million, or 55.3 percent of its initial increased FMAP grant awards.
  - Ohio officials indicated that they will use Recovery Act funds made available as a result of the increased FMAP to cover increased caseloads, offset general fund shortfalls due to state budget deficits, ensure compliance with prompt payment provisions, maintain existing populations, avoid eligibility restrictions, increase provider payments, and maintain and increase current levels of benefits.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Ohio was apportioned about \$935.7 million for highway infrastructure investment on March 2, 2009 by the U.S. Department of Transportation.
  - Of the \$935.7 million, about \$774.2 million was apportioned to the Ohio Department of Transportation (ODOT).
  - On March 26, 2009, ODOT announced that it will fund 149 projects with \$774.2 million in Recovery Act funding. According to ODOT officials, they are currently meeting with all project sponsors and performing detailed reviews of project documentation, confirming federal eligibility, assessing project delivery, and establishing project schedules.
  - As of April 16, 2009, the U.S. Department of Transportation had not obligated any Recovery Act funds for Ohio projects.
  - ODOT expects to begin advertising for bids during the week of April 20, 2009.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Ohio was allocated \$1,198,882 from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - As of April 17, 2009, Recovery Act funds for education and some child care programs had not been appropriated by the legislature. Officials with the Governor's office and Ohio's Office of Budget and Management (OBM) said these funds would be included in the budget for state fiscal years 2010-2011 and must pass by June 30, 2009.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments.
  - State officials said that they intend to apply for State Fiscal Stabilization Funds sometime in the future.

The state of Ohio expects to receive a total of \$8.2 billion from the Recovery Act over the next 3 years (fiscal years 2009-2011). In addition to the funding described above, Ohio is also receiving Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act (ESEA) (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA); and two programs of the U.S. Department of Agriculture—one for administration of the Temporary Food Assistance Program and one for competitive equipment grants targeted to low-income districts from the National School Lunch Program. The status of plans for using some of these funds is described in this appendix.

Before passage of the Recovery Act, Ohio created a Web site at [Recovery.Ohio.gov](http://Recovery.Ohio.gov), which represents the state's effort to create an open, transparent, and equitable process for allocating Recovery Act funds. Through the Web site, the state has encouraged proposals for uses of Recovery Act funds, and as of April 8, 2009, individuals and organizations from across Ohio have submitted over 23,000 proposals. While still receiving proposals, new submissions to the Web site have dropped in number dramatically, as guidance from federal agencies has clarified details about funding opportunities. By mid-April, approximately 26 state agencies with programmatic expertise had sorted the 23,000 submissions for response. Ohio regularly updates its Web site to provide timetables and information on applying for funds from state and federal agencies.

State agencies are beginning to identify specific projects to fund. On April 1, 2009, the Governor signed House Bill 2. As described by state officials, the bill appropriates \$1.9 billion in Recovery Act resources for 11 state agencies. According to state officials, additional appropriations are needed to spend Recovery Act funds for education and some child care programs, including Ohio's share of the State Fiscal Stabilization Fund. According to state officials, these appropriations are included in House Bill 1, which is part of the state's biennial budget and must be approved by June 30. As of April 1, 2009,

- The Ohio Department of Public Safety received about 730 proposals for Edward Byrne Memorial Justice Assistance Grant projects through the Ohio Recovery Web site. Applications for the state-administered funds are due on May 1, 2009; the department issued its request for proposals with caveats that specific reporting requirements are forthcoming from OMB and the U.S. Department of Justice.

- The Ohio Department of Job and Family Services (ODJFS) plans to allocate Workforce Investment Act (WIA) funds directly to local area workforce boards, and ODJFS provided these boards with estimates early so they could begin the planning process. Before funds were appropriated, some local areas began their efforts to procure providers for youth programs, particularly for work sites.

**Safeguarding and transparency:** Ohio is planning to use existing systems and safeguards to track Recovery Act funds, but reliance on subrecipients to provide data for enhanced reporting requirements may present challenges. For example, the fiscal year 2007 single state audit identified material weaknesses with a number of the systems that Ohio's Department of Jobs and Family Services uses to record and process eligibility and financial information for all their major federal programs. Moreover, officials with the Columbus Metropolitan Housing Authority (CMHA) noted limitations in how far they could reasonably be expected to track Recovery Act funds. They said they could track Recovery Act dollars to specific projects but could not systematically track funds spent by subcontractors on materials and labor.

**Assessing the effects of spending:** Ohio continues to explore ways to assess the impact of Recovery Act funds, but officials anticipate challenges. Specifically, in the absence of guidance on the types of data to collect, funding could be released before state officials have determined reporting requirements. Moreover, Ohio officials are concerned that, without uniform reporting requirements, each state will develop their own methodologies for assessing the impact of the federal stimulus, eliminating any possibility of making assessments that are comparable nationwide.

## Ohio Beginning to Use Recovery Act Funds

Ohio has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage (FMAP) Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher

federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

Ohio began the planning process to spend these funds before the enactment of the Recovery Act. In December 2008, to mitigate a budget revision<sup>3</sup> resulting from a 3.3 percent drop in estimated state tax revenues, the Governor's office assumed that additional federal assistance would be forthcoming. By including funds made available as a result of the increased FMAP in the assumptions used to revise the budget, cuts to state agency budgets and services were less severe. As of April 1, 2009, Ohio has drawn \$420.6 million in Medicaid Recovery Act funds or 55.3 percent of its initial FMAP funds. Ohio officials indicated that as of March 31, 2009, they will use Recovery Act funds to cover increased caseloads, offset general fund shortfalls due to state budget deficits, ensure compliance with

<sup>1</sup>Recovery Act, div. B, title V.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

<sup>3</sup>According to state officials, the Ohio constitution requires the state to have a balanced budget. Ohio's biennial budget covers two separate fiscal years which each begin on July 1 and end on June 30 of the following year. Separate budget bills are prepared for the state's General Revenue Fund and another for transportation and public safety activities. Because Ohio may not carry a deficit, the state must revise its budget whenever revenue estimates decline. Since enactment of its current budget for fiscal years 2008-2009, the Governor has made three downward revisions totaling over \$1.9 billion—or about 9.5 percent of the fiscal year 2009 State-only General Revenue Fund budget. These actions resulted in statewide cuts to agency and departmental budgets.

prompt payment provisions, maintain existing populations, avoid eligibility restrictions, increase provider payments, and maintain and increase current levels of benefits.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Ohio provided this certification, but conditioned it, noting that future highway spending would depend on: the state's collection of transportation revenues, state budgeting levels, ability to sell bonds, construction inflation, pending state legislation and the solvency of the federal highway trust fund.<sup>4</sup>

On March 26, 2009, the Governor announced that Ohio will fund 149 projects with \$774.2 million in Recovery Act funding. At least 113 of these projects, costing \$605.5 million, involve roadway repaving and bridge repair. Specific roadway projects range from \$200 million, for the Cleveland Innerbelt Bridge in Cuyahoga County, to \$50,000, for pavement markings in Belmont County. The remaining transportation funds, nearly \$170.0 million, are to be spent for railroad, maritime, intermodal, and engineering projects. ODOT officials told us that they are currently meeting with all project sponsors and performing detailed reviews of project documentation, confirming federal eligibility, assessing project delivery, and establishing project schedules. ODOT expects to begin advertising for bids during the week of April 20, 2009. In addition to the more than \$774 million apportioned to ODOT, another \$161.5 million was directly suballocated to Ohio's eight major metropolitan planning organizations in Akron, Canton, Cincinnati, Cleveland, Columbus, Dayton, Toledo, and Youngstown. As of April 16, 2009, the U.S. Department of

<sup>4</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.



Transportation had not obligated any Recovery Act funds for Ohio projects.<sup>6</sup>

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Ohio's initial SFSF allocation is \$1,198,882. According to state officials, the Ohio legislature has not passed the appropriations bills for Recovery Act-funded education programs and some child care programs. Those funds are expected to be appropriated, along with the rest of the state budget, by June 30, 2009. State officials said that they intend to apply for the State Fiscal Stabilization Funds sometime in the future.

To provide guidance on key Recovery Act requirements and assure that the state is maximizing its access to and use of Recovery Act funds, a number of statewide teams have formed to aid the planning process. The Governor's office organized a team of policy advisors, information technology specialists, and agency program staff to work on the application, program administration, reporting, and accountability related to the Recovery Act funds. This team is to ensure coordination with other offices, state agencies, or federal government entities and will work to ensure that Ohio appropriately applies for Recovery Act funding for which the state is eligible. In addition to the Governor's teams, Ohio's Office of Budget and Management (OBM) mandated that state agencies establish Recovery Act teams and recommended including fiscal, program, and compliance staff. The Governor also appointed an Infrastructure Czar to advise on the creation of an open, transparent process and to assist the state's leaders in the strategic use of infrastructure dollars. As the infrastructure awards moved toward completion, state officials said he has

<sup>6</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

turned his attention to assisting in competitive grant opportunities for entities in Ohio, including state agencies. The Czar will head a process for determining the most efficient and effective distribution of Recovery Act funds for competitive projects.

### Ohio Is Planning to Use Existing Systems and Safeguards to Track Recovery Act Funds, But Reliance on Subrecipients to Provide Data for Enhanced Reporting Requirements Could Present Challenges

The Ohio OBM will have primary responsibility for collecting and presenting financial data from state agencies through its Ohio Administrative Knowledge System (OAKS).<sup>6</sup> OBM has issued guidance to state agencies on Recovery Act reporting requirements and risk management and accountability responsibilities. To ensure that Recovery Act funds are segregated from other program funds and accounted for separately, OBM will create a centralized system to report all accounting data through OAKS. To facilitate tracking, OBM assigns an OAKS program number (for both revenues and expenses) unique to Recovery Act funds. OBM plans to develop a series of program reports that state agencies can use to regularly monitor Recovery Act revenues and spending metrics to ensure the agency is in compliance.

Although OAKS will allow the state to tag Recovery Act funding, in many cases the state agencies will rely on grantees and contractors to track the funds to the end use. Because the state intends to code each Recovery Act funding stream separately, and because these recipients typically manage more than one funding stream at a time, state officials said that the recipients should be able to track Recovery Act funds and other funding sources separately.

However, some state departments may not be able to rely on data from a number of the complex information systems they use. For example, the fiscal year 2007 single state audit identified material weaknesses with a number of the systems that ODJFS uses to record and process eligibility and financial information for all their major federal programs. Auditors found that without sufficient, experienced internal personnel possessing the appropriate technical skills to independently analyze, evaluate, and

<sup>6</sup>Ohio's fiscal year 2007 single audit report had a clean opinion on financial statements and did not identify any material weaknesses. In addition, on October 10, 2008, the Ohio Auditor of State issued a SAS 70 report on OAKS. While the Auditor noted numerous exceptions in the tests of operating effectiveness in the general control areas of program change and IT security, the Auditor opined that the state provided reasonable assurances that its controls (relevant to a user agency's internal controls) relating to financial statements, payroll, warrant writing, and electronic fund transfers (EFT) could be relied on, were suitably designed, and had been placed in operation as of June 30, 2008.

test these complex information systems, ODJFS management may not be reasonably assured these systems are processing transactions accurately. In its response, ODJFS replied that it did not have the resources to create a separate independent office, but said that it had protocols in place to provide some assurances that its systems were processing transactions accurately. State officials said they are aware of the weakness listed and are taking action to remedy it. Further, OBM has instructed its own internal audit office to provide additional resources to assist the agency.

Moreover, state and local officials we talked to raised some concerns about the ability of some localities to track Recovery Act funds to their end use. Specifically, they raised concerns about the capacity of grantees and contractors to track funds spent by subrecipients. For example, officials with the Ohio Department of Education said that they can track Recovery Act funds to school districts and charter schools, but they have to rely on the recipients' financial systems to be able to track funds beyond that. An official with the Columbus City Schools said that its accounting system might be challenged to meet enhanced reporting requirements. While they could provide assurances that Recovery Act funds were spent in accordance with program requirements, they could not report systemwide how each federal Recovery Act dollar was spent. Officials with the Columbus Metropolitan Housing Authority (CMHA) also noted limitations in how far they could reasonably be expected to track Recovery Act funds. They said they could track Recovery Act dollars to specific projects but could not systematically track funds spent by subcontractors on materials and labor. These officials added, however, that if they required the contractors to collect this information from their subcontractors, they would be able to report back with great detail. Still, without guidance from the federal government on specific reporting requirements, they were hesitant to burden their contractors with collecting the data.

On March 27, 2009, OBM directed state agencies to put in place risk management strategies for programs receiving Recovery Act funds. The guidance stresses the importance of having risk mitigation strategies in place that assure (1) management controls are operating to identify and prevent wasteful spending and minimize fraud, waste, and abuse; (2) adequate program monitoring by qualified personnel occurs; (3) awards are competed; (4) revenues and expenses are accurately reported; and (5) cost overruns and improper payments are minimized.

To ensure that existing safeguards are followed, OBM's Office of Internal Audit (OIA) plans to (1) provide training and education to state agency

personnel, (2) assess the adequacy and effectiveness of the current internal control framework, (3) test whether state agencies adhere to the current framework, and (4) coordinate multiagency reviews with both federal and state officials. According to OIA officials, pursuant to its statutory implementation plans, OIA will increase its internal audit staff from 9 (current) to 33 by transferring internal audit personnel from other state agencies and hiring new staff by July 2009. OBM officials said that the increase in OIA staff will help provide the needed resources to implement its objectives and ensure that current safeguards are in place and followed as the state manages its Recovery Act-funded programs.

Separately, both the Ohio State Auditor's office and the Ohio Office of Inspector General are to provide independent reviews of the use of Recovery Act funds. The Ohio State Auditor's office has created a Web-based database for all state agencies and local governments to report on Recovery Act funding and project expenditure activity. This database will also allow for public viewing of Recovery Act funds activity in the future. The State Auditor plans to use this information in helping assess risks and determine which programs to test as part of its single audit requirements. In addition, the State Auditor's office plans to conduct interim audit work over controls and compliance at various state agencies and local governments. According to state officials, as part of House Bill 2, the Ohio General Assembly created in the Office of Inspector General the position of Deputy Inspector General for funds received through the Recovery Act. The Deputy Inspector General is charged with monitoring state agency distribution of Recovery Act funds, conducting a program of random reviews of the processing of contracts associated with Recovery Act projects, and investigating all wrongful acts or omissions committed by officers, employees, or contractors.

### Ohio Is Exploring Ways to Assess Impact of Recovery Act Funds, but Officials Anticipate Challenges

OBM officials said that the emphasis on measuring the impact of certain Recovery Act funding has focused, thus far, on job creation; however, they noted that there are other goals of the Recovery Act. They argued that without comprehensive reporting guidance, states will struggle to assess impact on some of these other outcomes. States will not be able to go back later in the process to assess the impact of the Recovery Act on these other outcomes if they do not have guidance on what data to collect.

While some state agencies have identified options for reporting on job creation, there are concerns about the soundness of some of the methodologies. The Ohio Department of Transportation, for example, identified a study from 1979 which projects how many jobs will be created

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Appendix XVI: Ohio

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by a given expenditure. Other models have also been identified; however, in the absence of uniform guidance from the federal government, Ohio officials are concerned that states and localities will use a variety of methods that will ultimately not be comparable and will make nationwide assessment of the Recovery Act difficult.

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**Ohio's Comments on  
This Summary**


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We provided the Governor of Ohio with a draft of this appendix on April 17, 2009. The Chief Legal Council for OBM responded for the Governor on April 20, 2009. In general, the comments were either technical or were status updates. The Auditor of State also reviewed the draft and provided technical suggestions. We incorporated these comments, as appropriate.

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In addition to the contacts named above, Bill J. Keller, Assistant Director; Sanford F. Reigle, Analyst-in-Charge; Matthew Drerup; Laura Jezewski; Myra Watts-Butler; Lindsay Welter; Charles Willson; and Doris Yanger made major contributions to this report.

## Appendix XVII: Pennsylvania

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation and education programs. The three largest funding categories are the Medicaid increased Federal Medical Assistance Percentage (FMAP) grant awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, Centers for Medicare & Medicaid Services (CMS) had made about \$1 billion in increased FMAP grant awards to Pennsylvania.
  - As of April 3, 2009, Pennsylvania has drawn down about \$330.8 million, or nearly 32 percent of its initial increased FMAP grant awards.
  - Officials plan to use funds made available as a result of the increased FMAP grant awards to help cover the state's increased Medicaid caseload, ensure prompt claims payments, and to offset Pennsylvania's general fund budget deficit.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Pennsylvania was apportioned about \$1.0 billion for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated \$308.6 million for 108 Pennsylvania projects.
  - As of April 16, 2009, the Pennsylvania Department of Transportation had advertised competitive bids on 97 projects totaling about \$260 million, and the earliest contract was awarded on March 20, 2009.
  - These projects include activities such as highway repaving as well as bridge replacement and painting.
  - Pennsylvania will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund (Initial Release)**
  - Pennsylvania was allocated about \$1.3 billion from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increased teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. Pennsylvania plans to submit its application by April 25, 2009.
  - The Governor plans to use the funds to increase state funding for school districts and restore state funding for public colleges. The Governor also plans to use some funds to pay operating costs for the Department of Corrections.

## Appendix XVII: Pennsylvania

Pennsylvania is receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA) (commonly known as No Child Left Behind); programs under the Individuals with Disabilities Education Act (IDEA); Transit Capital Assistance and the Fixed Guideway Infrastructure Investment Programs; Workforce Investment Act; the U.S. Department of Housing and Urban Development Neighborhood Stabilization Program; the U.S. Department of Justice Edward Byrne Memorial Justice Assistance Grants; and the U.S. Department of Energy Weatherization Assistance Program. Plans to use these funds are described throughout this appendix.

**Safeguarding and transparency:** On March 4, 2009, the Governor named the Secretary of General Services as the state's Chief Implementation Officer responsible for the effective and efficient delivery of all Recovery Act-funded initiatives and projects. Additionally, the Governor set up a Recovery Management Committee to report to him on the progress of recovery efforts. According to the Chief Implementation Officer, this body meets regularly to discuss the status of the program, troubleshoot areas of concern, and report to the Governor on the progress of recovery efforts. In addition, Pennsylvania officials said they would use their existing integrated accounting system to track Recovery Act funds flowing through the state government. Although Pennsylvania has plans to publicly report its Recovery Act spending through a Web site ([www.recovery.pa.gov](http://www.recovery.pa.gov)), officials have said that the state may not be aware of all Recovery Act funds sent directly by the federal agencies to municipalities and independent authorities. In late March 2009, the Governor appointed a Chief Accountability Officer who will be responsible for reporting on Pennsylvania's use of Recovery Act funds. Pennsylvania plans to conduct several risk assessments for Recovery Act programs by June 2009. Pennsylvania's Auditor General also anticipates work auditing and investigating Recovery Act funds received by state and local agencies.

**Assessing the effects of spending:** Pennsylvania state departments are in the early stages of developing plans to assess the effects of Recovery Act spending. According to state officials, they are awaiting further guidance from the federal government, particularly related to measuring job creation.

## Pennsylvania Beginning to Use Recovery Act Funds

Pennsylvania has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 percent to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>2</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, Pennsylvania has drawn down \$330.8 million in increased FMAP grant awards, which is almost 32 percent of its awards to date.<sup>3</sup> Pennsylvania officials reported that they plan to use funds made available as a result of the increased FMAP to cover the state's increased Medicaid caseload and maintain current populations and benefits. State

<sup>1</sup>Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

<sup>3</sup>Pennsylvania received increased FMAP grant awards of \$1.04 billion for the first three quarters of federal fiscal year 2009.



officials also noted that such funds are allowing them to forgo reductions that they otherwise would have had to make because state funding streams are smaller this year. For example, Pennsylvania officials indicated that the state's share for Medicaid expenditures is 20 percent of their state revenues; thus this funding fluctuates as the economy rises and falls. Funding made available as a result of the increased FMAP will also be used to offset the state's general fund deficit and to help ensure that the Medicaid prompt payment requirements are met.<sup>4</sup> Pennsylvania officials noted that early notification from CMS regarding any reporting forms that the state will be required to complete would be beneficial to ensure that the state's accounting systems are properly aligned to produce needed reports.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and other surface transportation projects. States must follow the requirements for the existing program, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Pennsylvania provided the first of these certifications but noted that the state's level of funding was based on "planned non-bound state expenditures" (sic) and represented the best information available at the time of the state's certification.<sup>5</sup>

As of April 16, 2009, the U.S. Department of Transportation had obligated \$308.6 million for 108 Pennsylvania projects.<sup>6</sup> As of April 16, 2009, the

<sup>4</sup>To be eligible for the increased FMAP, states must comply with prompt pay requirements, which require states to pay 90 percent of clean claims from health care practitioners within 30 days of receipt and 99 percent of these claims within 90 days of receipt.

<sup>5</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>6</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term "obligation of funds" to mean the federal government's contractual commitment to pay for the federal share of a project. The commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

## Appendix XVII: Pennsylvania

Pennsylvania Department of Transportation (PennDOT) had advertised 97 projects for competitive bid totaling about \$260 million. These projects included highway repaving as well as bridge replacement and painting. Pennsylvania will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Pennsylvania's initial SFSF allocation is \$1.3 billion. According to the Chief Implementation Officer, Pennsylvania plans to file its application for these monies by April 25, 2009. According to the Governor's proposal, \$418 million in SFSF will support state funding to elementary and secondary schools and \$317 million to improve basic programs operated by local educational agencies in state fiscal year 2010. Similarly, \$44 million will help restore state funding for higher education. The Governor proposes to spend \$173 million on Department of Corrections operations in state fiscal year 2009 and reserve \$324 million for appropriation in fiscal year 2010.

**Some State Agencies and Localities Have Started Planning and in Some Cases Made Decisions for Using Recovery Act Funds**

Faced with declining revenue projections since fiscal year 2008, Pennsylvania officials believe that federal funds are critical to help alleviate the immediate fiscal pressure and help balance the state budget. Based on February 2009 projections, Pennsylvania faces a \$2.3 billion shortfall in fiscal year 2009, largely because of lower-than-expected revenues. Since September 2008, the Governor has cut state spending by more than \$500 million, imposed a state hiring freeze, and banned out-of-state travel and new vehicle purchases. Pennsylvania plans to draw \$250 million from the state rainy day fund—one-third of the current balance—to help avoid further cuts in fiscal year 2009.<sup>7</sup> According to Pennsylvania's

<sup>7</sup>Other actions to address the current shortfall include cuts in the enacted budgets for the legislature and independent agencies as well as increased revenue from natural gas drilling leases.

Secretary of the Budget, state revenues continue to decline and this may necessitate using even more rainy day funds during the current fiscal year. For fiscal year 2010, the Governor proposes to draw \$375 million from the rainy day fund. The Governor's budget proposal for fiscal year 2010, among other things, includes program cuts, layoffs, and reduced contributions for employees' health care. According to budget documents, federal fiscal relief would be used to prevent even deeper cuts throughout the budget. As part of the budget process, the Pennsylvania General Assembly generally must appropriate federal funds, including Recovery Act amounts.

The Governor's office and state agencies have begun planning for the use of Recovery Act funds in Pennsylvania. As noted previously, in March 2009, the Governor named a Chief Implementation Officer who is responsible for the effective and efficient delivery of all Recovery Act-funded initiatives and projects. According to the Chief Implementation Officer, the Recovery Management Committee meets regularly to discuss the status of the program, troubleshoot areas of concern, and report to the Governor on the progress of recovery efforts.<sup>8</sup> Pennsylvania plans to apply for competitive grants available under the Recovery Act, and the Governor's Secretary for Planning and Policy is coordinating this strategy.

Some state programs have received federal Recovery Act funds, and in some cases they have made funding decisions. For example, the U.S. Department of Transportation, through the Federal Highway Administration and the Federal Transit Administration, published final apportionments for the federal-aid highway program and Transit Capital Assistance and the Fixed Guideway Infrastructure Investment Programs March 2 and March 5, 2009, respectively.<sup>9</sup> PennDOT officials said that they have been working closely with metropolitan and rural transportation planning organizations to develop spending plans. On March 17, 2009, PennDOT released its final list of 241 highway and bridge projects to be

<sup>8</sup>The Recovery Management Committee is composed of: the Governor's Chief-of-Staff, the Chief Implementation Officer, the Chief Accountability Officer, the Secretary of Budget, Secretary of Policy, Secretary of Administration, Secretary of Legislative Affairs, and the Communications Director as well as other senior members of the Governor's administration.

<sup>9</sup>74 Fed. Reg. 9630 (March 5, 2009).

funded by the \$1.0 billion Recovery Act investment in highways.<sup>10</sup> Youth activities under the Workforce Investment Act have also received a funding allocation, and local Workforce Investment Boards must quickly establish summer youth programs for the Recovery Act Funding.<sup>11</sup> According to local officials in the Harrisburg region, planning challenges include identifying eligible youth (some of whom are out of school and difficult to locate), identifying employment opportunities that fit the requirements of the Recovery Act and the Workforce Investment Act, and performing required background checks on staff before the summer program begins.

The Pennsylvania Department of Education estimated allocations for their school districts while waiting for their final Recovery Act allocations. The Recovery Act funding will not be available to schools until the state General Assembly appropriates the funds.

**Some Programs Are Waiting for Clear Recovery Act Guidance and Some Have Questions about Using Funds for Administrative Purposes**

Program officials with whom we spoke provided varying levels of satisfaction with the guidance they had received from federal agencies, but some agencies were waiting for federal guidance to make spending and programmatic decisions. Officials from PennDOT stated that they have received guidance and have been able to administer Recovery Act funds. For the two new low-income housing tax credit financing programs created under the Recovery Act, the Pennsylvania Housing Finance Authority received initial information from the U.S. Department of Housing and Urban Development but no information from the U.S. Department of the Treasury; the housing finance agency is waiting for formal guidance before releasing implementation plans. Pennsylvania Department of Education officials also stated that although they received guidance on April 1, 2009, from the U.S. Department of Education on Recovery Act funds, they are concerned about certain provisions, such as

<sup>10</sup>PennDOT is also finalizing a list of transit projects to be funded from Recovery Act money. Of the approximately \$415 million in Recovery Act money apportioned by the Federal Transit Administration to Pennsylvania for transit capital assistance and fixed guideway infrastructure investment, about \$48 million (11.5 percent) will flow through the state to small urban (less than 200,000 population) and nonurbanized areas (less than 50,000 population). The remainder (about \$367 million) will go to large (over 200,000 population) areas directly.

<sup>11</sup>According to the U.S. Department of Labor guidance, the period of "summer" will be from May 1 through September 30 for purposes of the Recovery Act funds.

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the maintenance of effort provision, and are anticipating additional guidance.

Some agency officials were unclear about whether Recovery Act funds could be used to fund administrative costs. Even though a good portion of the Recovery Act funds is flowing through established grant programs, some state agency officials were concerned about paying for the increased administrative costs associated with program implementation, including increased reporting and tracking requirements. For example,

- Pennsylvania Department of Education officials were unclear if Recovery Act funds could be spent on state administrative costs and anticipated applying to the U.S. Department of Education for a waiver for these costs. State department officials were specifically concerned that they might need to build an entirely new reporting system to evaluate teachers and principals to meet Recovery Act requirements.
- Pennsylvania Department of Community and Economic Development officials said they had not received guidance from the U.S. Department of Housing and Urban Development about implementation of the Recovery Act portion of the Neighborhood Stabilization Program,<sup>12</sup> and were unsure of how much Recovery Act funds could be used for administrative purposes.
- PennDOT officials told us that, in some instances, non-Recovery Act funds were used to pay administrative costs for Recovery Act initiatives. This was the case in hiring two consultants to assess potential transit projects for Recovery Act funding.

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<sup>12</sup>The Neighborhood Stabilization Program was originally created in July 2008 by the Housing and Emergency Recovery Act of 2008 and was in the process of implementation when the Recovery Act increased program funding and made some of the funding subject to a competitive process to receive grants.

### Pennsylvania Developing Plans for Safeguards and Controls

Pennsylvania has entities responsible for tracking, monitoring, and overseeing financial expenditures. The Office of the Budget oversees the state's uniform accounting, payroll, and financial reporting systems. Pennsylvania is reorganizing and centralizing its internal audit and comptroller functions within the Governor's Office of the Budget.<sup>13</sup> The state's elected Treasurer has a pre-audit function to review disbursements to be paid out by state agencies prior to payment. The state Inspector General—who works for the Governor—is charged with investigating fraud, waste, abuse, and mismanagement. The state's elected Auditor General, who is responsible for ensuring that all state money is spent legally and properly, performs performance audits, financial audits, and investigations of state and local government entities. The Auditor General also partners with an accounting firm to perform Pennsylvania's annual single audit of the federal money that Pennsylvania receives to ensure the funds are spent according to federal laws and guidelines.

### Pennsylvania Has System to Track Recovery Act Funds, but Will Rely on Subrecipients to Meet Reporting Requirements at Local Level

Pennsylvania will use its existing accounting system to track Recovery Act funds and state officials are confident that it will adequately identify Recovery Act funds received and how they are used. Pennsylvania has an enterprise resource planning<sup>14</sup> (ERP) system that is used by all state agencies to account for federal and state funding. The integrated accounting system will be used to track Recovery Act funds. To accommodate the Recovery Act, on March 10, 2009, Pennsylvania's Office of the Budget issued an administrative circular to all agencies under the Governor's jurisdiction describing the specific accounting codes they must use to separately identify the expenditure of Recovery Act funds. Individual agencies are also taking action to ensure that Recovery Act funds are tracked separately. For example, PennDOT issued an administrative circular in March 2009 that established specific Recovery Act program codes to track highway and bridge construction spending. The department also established four new funds to account for Recovery Act fund reimbursements to local governments.

<sup>13</sup> According to the Secretary for Budget, the new reorganization will be completed in May 2009.

<sup>14</sup> An ERP solution is an automated system using commercial off-the-shelf software and consisting of multiple, integrated functional modules that perform a variety of tasks such as accounts payable, general ledger accounting, and grant management.

Pennsylvania officials said that the state will rely on subrecipients to meet reporting requirements at the local level. Recipients and subrecipients can be local governments or other entities such as transit agencies. For example, about \$367 million in Recovery Act money for transit capital assistance and fixed guideway infrastructure investment was apportioned directly to areas such as Philadelphia, Pittsburgh, and Allentown. State officials also told us that the state would not track or report Recovery Act funds that go straight from the federal government to localities and other entities, such as public housing authorities.

**Past Audits Have Identified Vulnerabilities, and Pennsylvania Plans to Identify and Assess Risks Associated with Recovery Act Funds**

Past audits have identified vulnerabilities in Pennsylvania's financial reporting and noncompliance with requirements for federal money. Pennsylvania's fiscal year 2007 single audit report had an unqualified opinion on financial reporting, but auditors found material weaknesses in the accounting controls. For example, auditors found weaknesses in segregating duties among staff and monitoring user activities to reduce the risk of inappropriate changes to accounting data or misappropriation of assets. Pennsylvania's Secretary of the Budget told us that to mitigate this risk, internal auditors now are to work closely with the Office of Administration and the Office of Information Technology on all new system changes to ensure internal controls are built into the application. The single audit scope was limited in that auditors could not obtain key documentation needed to check compliance with procurement regulations for competitively bid contracts for goods and services. The Secretary of the Budget told us that, beginning in January 2009 under Pennsylvania's Right to Know law, information related to losing bids and scoring by participants of the procurement committees will now be available for audit purposes.

In 2007, Pennsylvania had a qualified opinion due to noncompliance with major federal programs. For example, auditors identified 13 weaknesses in which state agencies, such as the Department of Community and Economic Development, did not adequately monitor subrecipients or failed to document procedures for performing on-site monitoring for subrecipients or subgrantees. It is important to correct these weaknesses for Pennsylvania to be able to provide reasonable assurance that its subrecipients comply with requirements for Recovery Act funding, when appropriate. Pennsylvania's Secretary of the Budget told us that the Office of Budget monitors the agencies' corrective action plans and provides additional program monitoring and training for agency program staff as appropriate. As of April 2009, the Office of the Budget's auditors were

reviewing the status of implementing corrective action plans for past single audit findings.

Pennsylvania officials also cited potential risks, based on experience with existing structures, with programs receiving Recovery Act funding. Pennsylvania's Governor told us that he is concerned that school districts may use Recovery Act funds to start or expand education programs that are fiscally unsustainable when the federal funds expire. Several Pennsylvania officials, including the Governor, were specifically concerned about the Weatherization Assistance Program. Under the Recovery Act, the program is receiving a significant increase in funding and will make substantial use of contractors to weatherize properties. A 2007 Pennsylvania Auditor General report found that the program had, among other things, weak internal controls, weaknesses in contracting, and inconsistent verification and inspection of subcontractor work.<sup>15</sup>

According to the Chief Implementation Officer, Pennsylvania plans to conduct several risk assessments by June 2009, including assessments of potential contractor capacity challenges for transportation projects and the capacity of current weatherization providers and contractors. The Office of Chief Counsel is reviewing all construction contracts and grants to ensure compliance with the Recovery Act requirements as well as guidance issued by the U.S. Office of Management and Budget (OMB) and federal agencies. According to Pennsylvania's Secretary of the Budget, the new Bureau of Audits within the Office of the Budget will develop a risk-based approach for Recovery Act audits with measurable criteria and develop a matrix of risks for each Recovery Act program by the end of June 2009.

#### Plans for Oversight and Transparency of Pennsylvania's Recovery Act Funds

Pennsylvania has established structures to oversee Recovery Act funds and provide transparency to the public. On March 31, 2009, the Governor appointed a Chief Accountability Officer who will be responsible for reporting on Pennsylvania's use of Recovery Act funds and working with the Office of Budget to ensure funds are spent in accordance with

<sup>15</sup>Pennsylvania Auditor General, *A Special Performance Audit of the Department of Community and Economic Development's Weatherization Assistance Program*, August 2007.



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Recovery Act requirements.<sup>16</sup> To serve as a portal for transparency of state Recovery Act spending, Pennsylvania also established a Web site ([www.recovery.pa.gov](http://www.recovery.pa.gov)) that makes available updates on funding and solicits public input on funding use. The Chief Accountability Officer will be responsible for identifying ways to present visual evidence, such as photographs and mapping, to help citizens track Recovery Act projects in Pennsylvania.

A new Pennsylvania Stimulus Oversight Commission was created by the Governor—by executive order on March 27, 2009—after outreach to the Pennsylvania congressional delegation, the state legislature, and others. In addition to the Chief Accountability Officer, the commission is composed of the Governor, the Recovery Act Chief Implementation Officer, four representatives selected by Pennsylvania's congressional delegation, members of each of the four caucuses in Pennsylvania's General Assembly, and representatives from the Pennsylvania Chamber of Business and Industry, United Way of Pennsylvania, and Pennsylvania AFL-CIO. The commission was established to, among other things, monitor Pennsylvania's efforts to ensure compliance with the Recovery Act and to review the state's approach to allocating and disbursing funds, tracking funds, transparency, performance, and grants management and oversight. The commission met for the first time on March 31, 2009, and has not announced its oversight plans; the next commission meeting will be on April 23, 2009.

Other state offices are generally not expecting new staff or resources for Recovery Act oversight. The Auditor General anticipates work auditing and investigating Recovery Act funds received by state and local agencies. For example, the Auditor General will audit Recovery Act funds during the annual single audit and will initiate additional compliance audits for Recovery Act programs. The Auditor General observed that the Recovery Act did not provide funding for his office to undertake work related to the act. In addition, officials of the Auditor General's office have different views about what authority they have to audit federal money that flows directly to localities, such as housing authorities and municipalities. Pennsylvania is also in the process of reorganizing and centralizing its internal audit and comptroller functions within the Governor's Office of

<sup>16</sup>The Chief Accountability Officer also will chair a new Governor's Working Group for Stimulus Accountability that includes the Chief Implementation Officer and senior state officials. In addition, the Chief Accountability Officer also serves on the Governor's Recovery Management Committee.

the Budget. According to the Secretary of Budget, the Bureau of Audits is not expected to dramatically change audit responsibilities in the state but rather provide a more focused, risk-based approach, particularly for Recovery Act funding. This office is expected to employ 95 people, about 70 of whom will be field auditors. The remaining staff will be responsible, among other things, for subrecipient desk reviews and agency risk assessments.

The number of staff devoted to program oversight, and implementation in some state agencies has been affected by the state's hiring freeze. For example, Workforce Investment Act program officials said monitoring efforts will need to increase under the Recovery Act and they have applied to the Governor for a waiver to hire additional staff. Department of Community and Economic Development officials told us that they have requested to hire 12 people, 3 or 4 of whom will be devoted to Recovery Act work related to the Neighborhood Stabilization Program. The Pennsylvania Commission on Crime and Delinquency, which administers the Edward Byrne Memorial Justice Assistance Grants, is trying to maximize the use of its existing staff and sought advice from the U.S. Department of Justice Inspector General; the latter will give a presentation, share checklists, and train program staff in monitoring subrecipients. PennDOT officials told us that they meet weekly to oversee the highway and bridge program funded through the Recovery Act. These meetings cover such things as the status of obligating program funds and potential problems. The department also has a special "war room" that tracks each project in each state district.

### Plans to Assess Impact of Recovery Act Funds Depend on Federal Guidance

Agency officials stated that, although they are emphasizing the planning and allocating of Recovery Act funds quickly, they are aware of requirements to assess the economic and other impacts of these funds. The new Chief Accountability Officer will be responsible for developing and using performance measures to demonstrate outcomes associated with Recovery Act spending and projects. Some agency officials with whom we met—at the Pennsylvania Department of Education and the Department for Community and Economic Development—are generally waiting for additional guidance from the federal government on performance measures, especially on how to measure and report jobs created and sustained.

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**Pennsylvania's  
Comments on This  
Summary**

We provided the Governor of Pennsylvania with a draft of this appendix on April 17, 2009. The Chief Implementation Officer and the Secretary of the Budget responded for the Governor on April 20, 2009. These officials provided clarifying and technical comments that we incorporated where appropriate. We also provided the Auditor General's staff with portions of the draft that addressed the Auditor General's past work and plans related to Recovery Act funding. We incorporated those technical comments as appropriate.

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## Appendix XVIII: Texas

### Overview

**Use of funds:** An estimated 90 percent of fiscal year 2009 Recovery Act funding provided to states and localities will be for health, transportation, and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, the State Fiscal Stabilization Fund, and highways.

- ✓ **Medicaid Federal Medical Assistance Percentage (FMAP) Funds**
  - As of April 3, 2009, the Centers for Medicare & Medicaid Services (CMS) had made approximately \$1.45 billion in increased FMAP grant awards to Texas.
  - As of April 1, 2009, the state has drawn down about \$665.7 million, or 46 percent, of its initial increased FMAP grant awards.
  - Texas officials noted that the funds made available as a result of the increased FMAP will allow the state to maintain the program's level of service and eligibility standards in fiscal year 2009.
- ✓ **Transportation—Highway Infrastructure Investment**
  - Texas was apportioned about \$2.25 billion for highway infrastructure investments on March 2, 2009, by the U.S. Department of Transportation.
  - As of April 16, 2009, the U.S. Department of Transportation had obligated \$533.7 million for 159 projects in Texas.
  - According to Texas Department of Transportation officials, the department is scheduled to receive bids in April 2009 on 137 contracts that would total approximately \$400 million in Recovery Act funds.
  - Texas will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.
- ✓ **U.S. Department of Education State Fiscal Stabilization Fund**
  - Texas was allocated about \$2.66 billion from the initial release of these funds on April 2, 2009, by the U.S. Department of Education.
  - Before receiving the funds, states are required to submit an application that provides several assurances to the Department of Education. These include assurances that they will meet maintenance of effort requirements (or that they will be able to comply with waiver provisions) and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. According to Texas officials, the state's application likely would not be submitted before the state legislature (which is in session until June 1, 2009) has finalized an appropriation for public and higher education.
  - Texas officials indicated that the state plans to use its allocated federal funds to assist in continuing the historical levels of support for elementary, secondary, and higher education in the state. Education Agency officials said funds could be used, for example, to support efforts related to assessing school performance, teacher incentives, and teacher equity. Higher education officials anticipate using the funds to mitigate tuition and fee increases; support modernization, repair, and renovation of facilities; and provide incentive funding based on degrees awarded.

## Appendix XVIII: Texas

Texas is receiving additional Recovery Act funds under other programs, such as programs under Title I, Part A of the Elementary and Secondary Education Act (ESEA), commonly known as No Child Left Behind; programs under the Individuals with Disabilities Education Act (IDEA); two programs of the U.S. Department of Agriculture—one for the administration of the Temporary Food Assistance Program and one for competitive equipment grants targeted to low income districts from the National School Lunch program; housing programs, including weatherization assistance; and justice assistance grants. The status of plans for using selected funds is discussed throughout this appendix.

**Safeguarding and transparency:** To help ensure accountability and transparency, the Texas legislature's forthcoming general appropriations act—expected to be passed by June 2009 to function as the state's fiscal 2010-2011 biennium budget—will have a provision for tracking Recovery Act funds allocated to the state, according to the executive and legislative branch officials we contacted in Texas. To provide additional accountability and transparency, the Comptroller of Public Accounts has established a centralized budget account (with a unique funding code) for Recovery Act funds and has also established a Web page, [www.window.state.tx.us/recovery](http://www.window.state.tx.us/recovery), with links to [www.recovery.gov/](http://www.recovery.gov/). To further help ensure accountability and transparency, Texas officials suggested that federal authorities provide concurrent notification to the state's key stakeholders—particularly the Office of the Governor, the Comptroller of Public Accounts, the State Auditor's Office, and the Legislative Budget Board<sup>1</sup>—when Recovery Act funds are periodically distributed to Texas agencies and/or localities. Also, Texas officials told us that despite U.S. Office of Management and Budget (OMB) guidance, the increased FMAP funds the state has received through the Recovery Act, to date, have not been separately identified by the federal government.

**Assessing the effects of spending:** Texas officials commented that—under the state's performance-based budgeting process—agencies already have measures in place for assessing the performance of programs. Officials also believe that the state's current monitoring and control

<sup>1</sup>According to state officials, the Legislative Budget Board is a permanent joint committee of the Texas legislature that develops budget and policy recommendations for legislative appropriations for all agencies of state government, as well as completes fiscal analyses for proposed legislation. The lieutenant governor and House speaker serve as co-chairs of the board. Other members include the chairs of the House Appropriations Committee and the Senate Finance Committee. See [www.lbb.state.tx.us](http://www.lbb.state.tx.us).

processes and procedures are adequate to administer initiatives funded under the Recovery Act. The officials recognized, however, that some adjustments to performance measures may be needed for assessing the impact of Recovery Act funds.

### Texas Beginning to Use Recovery Act Funds

Texas has begun to use some of its Recovery Act funds, as follows:

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>2</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.<sup>3</sup> Generally, for federal fiscal year 2009 through the first quarter of federal fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs, (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs, and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

<sup>2</sup>Recovery Act, div. B, title V, § 5001.

<sup>3</sup>Although the Recovery Act was enacted February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

As of April 1, 2009, Texas had drawn down \$665,665,000, or 46 percent, of its initial increased FMAP grant awards of \$1,448,824,000 in FMAP funds. Texas officials commented that the funds made available as a result of the increased FMAP will allow the state to maintain the program's level of service and eligibility standards and cover increased caseloads, among other uses. Texas officials indicated that guidance from CMS is needed regarding whether certain programmatic changes being considered by Texas, such as a possible extension of the program's eligibility period, would affect the state's eligibility for increased FMAP funds.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor must certify that the state will maintain its current level of transportation spending, and the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds. Texas provided this certification but noted that the state's level of funding was based on the best information available at the time of the state's certification.<sup>4</sup>

Texas was apportioned about \$2.25 billion of Recovery Act funds for highway infrastructure investments on March 2, 2009, by the U.S. Department of Transportation. As of April 16, 2009, the U.S. Department of Transportation had obligated \$533.7 million of Recovery Act funds for 159 projects in Texas.<sup>5</sup> According to Texas Department of Transportation officials, the department is scheduled to receive bids in April 2009 on 137 contracts that would total approximately \$400 million in Recovery Act

<sup>4</sup>A number of states qualified their certifications in various ways. The legal effect of such qualifications is currently being examined by the U.S. Department of Transportation and has not been reviewed by GAO.

<sup>5</sup>For federal-aid highway projects, the Federal Highway Administration of the U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of a project. This commitment occurs at the time the federal government approves a project agreement and the project agreement is executed.

funds. Texas will request reimbursement from the U.S. Department of Transportation as the state makes payments to contractors.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other things, it will take actions to meet certain educational requirements such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

Texas' initial SFSF allocation is \$2,662,203,000. According to Texas officials, the state generally plans to use its SFSF allocation to assist in continuing the historical levels of support for elementary, secondary, and higher education in the state. In April 2009, officials from the Office of the Governor informed us that the state was in the process of preparing its application for submission to the U.S. Department of Education—and that the application would reflect the fact that providing funding for public education is a priority in the state. The officials noted that the state's application likely would not be submitted until the state legislature (which is in session until June 1, 2009) has finalized an appropriation for elementary, secondary, and higher education. Also, the officials commented that the state was awaiting further federal guidance on the appropriate use of Recovery Act funds. Generally, however, Texas Education Agency officials said that the federal funds could be used, for example, to support efforts related to high-quality assessment performance in schools, teacher incentives, and teacher equity. Also, according to the Texas Higher Education Coordinating Board, public institutions of higher education in Texas anticipate expending Recovery Act funds for three purposes—mitigating tuition and fee increases; supporting modernization, repair, and renovation of facilities; and providing incentive funding based on degrees awarded. To provide tracking and oversight of the Recovery Act funds, board officials commented that existing systems for implementing policies for accountability, internal controls, compliance, and reporting would be leveraged to the maximum extent possible to avoid the administrative burden associated with creating a completely new system. These officials explained that the proposed uses of the Recovery Act funds are not dissimilar to other well-established programs within the agency.



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Overall, throughout the multiyear time frame covered by the Recovery Act, Texas' share of the total federal funds is estimated to be more than \$15 billion for supporting a variety of program areas, such as health and human services, state fiscal stabilization, transportation, and education. (See table 9.)

**Table 9: Estimated Allocations by Program Areas of Federal Recovery Act Funds in Texas (as of March 2009)**

Program areas	Estimated federal Recovery Act funds (through fiscal year 2011)	
	Amount (in billions)	Percentage of total
Health and human services: Of the \$4.5 billion, a large majority (\$4.2 billion) is an increase in the Federal Medical Assistance Percentage funds.	\$4.5	29
State fiscal stabilization funds: Of the \$4.0 billion, about 82 percent (\$3.3 billion) is to be used to support elementary, secondary, and higher education (e.g., for the purposes of modernization, renovation, and repair). The other 18 percent of the funds may be used, at the discretion of the governor, for education, public safety, and other government services.	4.0	26
Transportation: Of the \$2.8 billion, a large majority (\$2.3 billion) is to be allocated for highway and bridge construction.	2.8	18
Education: Of the \$2.3 billion, a large majority involves two formula grant programs—grants to local educational agencies (\$1.2 billion) and special education grants to assist individuals with disabilities (\$1.0 billion).	2.3	15
Housing and infrastructure: Of the \$1.2 billion, the largest component (\$327 million) is the weatherization assistance program to provide energy-related improvements to homes and educate residents about energy conservation.	1.2	8
Other: Program areas include, for example, Edward Byrne Memorial Justice Assistance Grants (\$147.5 million) and child care and development block grants (\$214.9 million).	0.6	4
<b>Total</b>	<b>\$15.4</b>	<b>100%</b>

Source: GAO summary based on review of Texas Legislative Budget Board data and interviews with agency officials.

Note: The amounts of Recovery Act funds shown in the table are anticipated to flow to or through Texas agencies. As such, Texas plans to include these Recovery Act funds in the state's budget-setting process, as discussed below. However, additional amounts of other Recovery Act funds (not yet quantified) are anticipated to flow directly to localities within the state.

In his letter certifying acceptance of federal Recovery Act funds, the Texas Governor voiced opposition to "using these funds to expand existing government programs, burdening the state with ongoing expenditures long after the funding has dried up."<sup>6</sup> Similarly, during our review in Texas, legislative branch officials generally acknowledged that most of the

<sup>6</sup>State certification letter, dated February 18, 2009, from Governor Rick Perry, State of Texas, to President Barack Obama.

federal Recovery Act funds appear to be one time in nature and that the state must avoid spending the funds for ongoing projects that would result in unsustainable future costs to the state's budget. An illustration of such avoidance involves unemployment insurance. While the Texas Governor accepted some Recovery Act funds for unemployment insurance, he did not request Unemployment Insurance Modernization funds because the Governor believed that receiving those funds would place additional tax burdens on businesses, which would impede job creation and hamper the economy.<sup>7</sup>

Even though Texas generally continues to fare better economically than most states, nearly all available data suggest that the Texas economy is in recession, according to the Federal Reserve Bank in Dallas. In January 2009, the Office of the Comptroller of Public Accounts reported that the state's fiscal 2010-2011 biennium budget will have \$9 billion less in revenue than the current biennium budget. For perspective, officials with the Governor's office told us that the \$9 billion represents a 5 percent adjustment to the budget.

In January 2009, anticipating that Texas faced a likely budget shortfall, the co-chairs of the state's Legislative Budget Board requested that state agencies look for ways to reduce fiscal year 2009 expenditures by 2.5 percent. The co-chairs further noted that the state legislature should prudently plan on having a reasonable reserve in the state's economic stabilization fund<sup>8</sup> so that the state does not face a large deficit in the next biennium, ending August 31, 2011. In response to the co-chairs' request for ways to reduce spending in fiscal year 2009, state agencies identified approximately \$396 million in potential budget reductions based on hiring freezes, reduced services, delayed capital purchases, and other cost-cutting efforts. At the time of their request, the co-chairs noted that the Recovery Act—which was being debated in Washington, D.C.—could not

<sup>7</sup>According to the Texas Comptroller of Public Accounts Web site, in order to accept Unemployment Insurance Modernization Funds under the Recovery Act the state would be required to change its eligibility standards to expand benefits to additional categories of workers. State officials described a recently introduced, but not enacted, bill in the Texas legislature to propose changes to the eligibility standards. On April 20, 2009, the Texas Senate voted in favor of the bill. According to those officials, if the House of Representatives also votes in favor of the bill, the governor has the option of vetoing the bill.

<sup>8</sup>The state's economic stabilization fund is commonly referred to as the "rainy day fund." The fund balance, according to Legislative Budget Board estimates, is expected to reach \$9.1 billion by 2011.

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responsibly be factored into the state's budget process because many details were not known.

In discussions with our review team in March 2009, representatives of the Office of the Lieutenant Governor commented that because of Recovery Act funds, state agencies were not required to implement the 2.5 percent spending reductions anticipated for state fiscal year 2009 and, further, the state did not have to tap into its rainy day fund. The representatives told us that absent the availability of Recovery Act funds, state agencies likely would have been asked to make cuts of about 10 percent for the fiscal 2010-2011 biennium budget, in addition to the state drawing upon the rainy day fund.

On the other hand, officials representing the Office of the Governor commented that budget deficit situations do not necessarily result in the state using its rainy day fund. The officials stressed that—to meet the requirement to pass a balanced budget—a variety of other solutions could be considered, such as budget reallocations among state agencies and programs, as well as spending cuts. As an example, these officials noted that even though the state's overall budget was reduced in 2003, the state raised education spending by \$1 billion that year. Additionally, the officials explained that use of the rainy day fund is not an option readily available because it requires approval by two-thirds of the state legislature.

### Texas Is Taking Steps to Help Ensure Accountability and Transparency and Address Potential Areas of Vulnerability

Texas is taking various steps to help ensure accountability and transparency and address areas of vulnerability potentially associated with Recovery Act spending.

#### Steps to Help Ensure Accountability and Transparency

Texas officials noted that Recovery Act funding will flow generally through existing federal-state agency partnerships or programs. Thus, to the extent possible, the state plans to use existing systems, processes, or mechanisms to provide Recovery Act funding accountability and transparency, according to the executive and legislative branch officials we contacted in Texas. In further reference to accountability and transparency, oversight of federal Recovery Act funds in Texas involves various stakeholders, including the Office of the Governor, the State

Auditor's Office, and the Office of the Comptroller of Public Accounts as well as two entities established within the Texas legislature specifically for this purpose—the House Select Committee on Federal Economic Stabilization Funding<sup>9</sup> and the House Appropriations' Subcommittee on Stimulus. Also, according to executive and legislative branch officials in Texas, the state plans to ensure that the forthcoming biennial general appropriations bill has a provision designed to specifically facilitate the tracking of federal Recovery Act funds distributed to Texas—that is, the act will have a separate section ("article") that identifies, by applicable state agency, Recovery Act funds allocated to Texas.<sup>10</sup> At the time of our study in April 2009, the Texas legislature was in session (81st regular session) and had not finished its work to complete and submit to the Governor a general appropriations bill for the state's fiscal 2010-2011 biennium (Sept. 1, 2009, through Aug. 31, 2011).<sup>11</sup>

To further facilitate tracking, in March 2009, the Office of the Comptroller of Public Accounts established a centralized budget account for federal

<sup>9</sup>See [www.txstimulusfund.com](http://www.txstimulusfund.com). The committee chair has been holding hearings with state agencies and asking about the resources they have or need; how the Recovery Act funds will be disbursed; and what policies, procedures, and internal controls are in place for the funds.

<sup>10</sup>Essentially, as described by state officials, the Texas legislature will use the state's general appropriations bill to appropriate federal Recovery Act funds for the fiscal 2010-2011 biennium (Sept. 1, 2009, through Aug. 31, 2011). Any Recovery Act funds received earlier (i.e., funds received in fiscal year 2009) will not be included in the general appropriations bill. In Texas, according to state officials, the general appropriations bill functions as the state's budget by allocating resources and setting performance targets based on the strategies identified by agencies in their respective strategic plans. Under Texas law, the governor is the state's chief budget officer, but the state legislature and the Legislative Budget Board have a large role in the state's budget process. By constitutional mandate, Texas operates under budgets set for 2-year periods. Both the governor and the Legislative Budget Board develop budget recommendations and submit budget proposals to the legislature, which adopts a budget (general appropriations bill) for the 2-year period. The state legislature is constitutionally required to pass a balanced budget, and the governor is constitutionally required to sign a balanced budget.

<sup>11</sup>According to state officials, the legislature meets in regular session for 140 days in odd-numbered years. The 81st regular session began January 13, 2009, and extends to June 1, 2009. The House and Senate generally take turns originating the general appropriations bill and chairing the budget conference committee. Both chambers work on the budget and hold hearings simultaneously. After the general appropriations bill has been approved by both chambers of the legislature, it must be certified by the Comptroller of Public Accounts; thereafter, it is submitted to the governor for approval. The governor has line item veto power, which allows the governor to veto specific appropriations rather than vetoing the entire bill. A veto may be overridden by a two-thirds vote in each chamber of the legislature.

Recovery Act funds, with a unique funding code (0369).<sup>12</sup> In turn, according to Texas officials, state agencies are modifying their financial systems to enable tracking of Recovery Act funds. Also, after the Recovery Act passed, the Office of the Governor began hosting regularly scheduled meetings (twice weekly) of a Stimulus Working Group comprising representatives of major state agencies to help ensure statewide communication of the need for accountability and transparency regarding Recovery Act funds.<sup>13</sup> Similarly, a periodic forum of the internal audit staff of Texas state agencies serves as another means of statewide communication.<sup>14</sup> Also, in March 2009, the Office of the Comptroller of Public Accounts scheduled training regarding federal awards and financial statements—training that included representatives from the Office of the Governor to discuss Recovery Act funds. Further, the Comptroller's Office plans to hire 5 to 10 additional staff to help account for Recovery Act funds, according to office officials. In April 2009, the Comptroller's Office issued policies and procedures to state agencies related to use and subsequent reporting on Recovery Act funds.

The State Auditor's Office is taking additional steps to ensure accountability. Anticipating that federal Recovery Act funding will increase its scope of responsibilities, the State Auditor's Office plans to hire 10 additional staff (9 auditors and 1 investigator).<sup>15</sup> The office intends to audit Recovery Act funds through the Single Audit of the State of Texas' expenditures of federal awards—that is, the audit required by the Single Audit Act and to which OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, relates.<sup>16</sup> Also, the State

<sup>12</sup>Also, the Office of the Comptroller of Public Accounts has established a stimulus-related Web page ([window.state.tx.us/recovery/](http://window.state.tx.us/recovery/)) with links to the national Web site, [www.recovery.gov](http://www.recovery.gov).

<sup>13</sup>Members of GAO's review team attended the March 19, 2009, meeting of the Stimulus Working Group in Austin, Texas.

<sup>14</sup>Members of GAO's review team attended the March 27, 2009, state agency internal audit forum in Austin, Texas.

<sup>15</sup>State officials described the State Auditor's Office as the independent auditor for Texas state government. The office operates with oversight from the Legislative Audit Committee, a six-member permanent standing committee of the Texas legislature, jointly chaired by the lieutenant governor and the speaker of the House of Representatives.

<sup>16</sup>For example, see State Auditor's Office, *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2008*, SAO Report No. 09-330 (Austin, Tex., Feb. 2009).

Auditor's Office may conduct discretionary audits based, for example, on (1) discussions with internal auditors at state agencies or (2) risk assessments that consider previously reported material weaknesses in program compliance and internal controls, as well as risk assessments of programs that have not been tested before. Furthermore, the State Auditor's Office noted that, as warranted, it pursues leads generated by complaint letters, hotline calls, and other information received from the public. In this regard, the State Auditor's Office has Web-based and telephone "hotline" contacts for the general public to use in reporting possible fraud, waste, and abuse. In March 2009, the State Auditor told us that he was preparing a letter to send to state agencies regarding their general fraud responsibilities related to state funds.<sup>17</sup> Moreover, in April 2009, the State Auditor's Office informed us that a provision for reporting Recovery Act-related fraud is being added to the state's fiscal 2010-2011 biennium appropriations bill. Among other requirements, this legislative provision, according to the State Auditor's Office, will require that state agencies' Web sites provide information on how to report suspected fraud, waste, and abuse directly to the State Auditor's Office.

According to state officials, in March 2009, a bill was filed in the Texas legislature that proposed creating a new office—the Texas Fiscal Responsibility Office—to oversee or monitor the spending of federal Recovery Act funds in Texas.<sup>18</sup> As of early April 2009, the bill's status had not been determined by the state legislature, which was scheduled to be in regular session until June 1, 2009.

#### Potential Areas of Vulnerability of Recovery Act Funds in Texas

In response to our inquiry, the State Auditor's Office provided us its views regarding accountability risks and other challenges potentially associated with the expenditure of federal Recovery Act funds in Texas. Based on its experience in auditing Texas' use of previous federal awards and reporting internal control deficiencies or material weaknesses, the State Auditor's Office noted that relatively high risks generally can be anticipated with certain types of programs—such as (1) new programs with completely

<sup>17</sup>Some Texas agencies, such as the Health and Human Services Commission, have an Office of Inspector General.

<sup>18</sup>State officials identified this bill as H.B. No. 2942, cited as the "Texas Government Accountability and Transparency Act of 2009." According to state officials, under the bill's provisions, the Texas Fiscal Responsibility Office would be created as an independent agency of the legislative branch of state government.

new processes and internal controls, (2) programs that lack clear guidance on allowable uses of Recovery Act funds, (3) programs that distribute significant amounts of funds to local governments or boards, and (4) programs that rely on subrecipients for internal controls and monitoring. The State Auditor's Office also noted that general economic stability and public education programs are considered to be high risk because they are new programs and federal guidance regarding the state's appropriate use of the funds the funds is uncertain. The State Auditor's Office further noted that highway construction and workforce programs are also high risk because funds flow through contractors or to local entities, respectively.<sup>19</sup>

Officials from Office of the Governor acknowledged that there are inherent risks associated with large, complex programs as well as programs that involve a large number of contracts and rely on subrecipients. However, the officials emphasized that Texas has experience in monitoring these types of programs, and officials noted that state agencies have controls in place to mitigate these risks. Regarding the Medicaid program, for example, the officials noted that in 2003, the Governor appointed an Inspector General for the Texas Health and Human Services Commission and charged the Inspector General with monitoring and preventing fraud, waste, and abuse. Also, the officials noted that the state's Attorney General's Office has a Medicaid Fraud Investigation Unit.

The Texas State Auditor's Office made a recommendation regarding the monitoring of subrecipients for risk in its most recent audit of the Texas Education Agency.<sup>20</sup> The audit report did not find that subrecipients were improperly spending federal funds or were not meeting federal requirements; however, the report did note, however, that the agency had "a limited number of resources available to monitor fiscal compliance." The audit report recommended that the Texas Education Agency continue to add resources, within its budget constraints, to increase its monitoring of federal fiscal compliance performed. According to the State Auditor's Office, following the audit in February 2009, the Texas Education Agency

<sup>19</sup>The State Auditor's Office further noted that additional information about high-risk programs could be obtained by inquiring about what actions at the agency level that management will be taking to mitigate risks.

<sup>20</sup>State Auditor's Office, *State of Texas Federal Portion of the Statewide Single Audit Report for the Fiscal Year Ended August 31, 2008*, SAO Report No. 09-330 (Austin, Tex., Feb. 2009). The audit was performed by an independent public auditing firm under contract to the State Auditor's Office.

created a comprehensive correction plan, which the agency is implementing to address this resource issue.

After the Recovery Act was enacted, the Texas Education Agency announced in March 2009 that it was creating a task force on federal stimulus and stabilization to coordinate the agency's plans. Also in March 2009, the agency reported that it had established new accounting codes for tracking Recovery Act funds. Furthermore, the agency indicated that its application guidance for the temporary funding would specify that (1) grantees are expected to expend funds in ways that do not result in unsustainable continuing commitments after the funding expires and (2) the funds must be separately tracked and monitored.

Generally, state officials recognized that a potential vulnerability can be associated with significant increases in funding levels. An example is the weatherization assistance program. As noted in table 1, of the estimated \$1.2 billion in Recovery Act funds to be used for housing and infrastructure programs in Texas, weatherization assistance is the largest component program in terms of funding (\$327 million). This funding level represents about a 25-fold increase over the estimated annual amount (\$13 million) that existed before the Recovery Act, according to Texas Department of Housing and Community Affairs data. Tentatively, the department indicated that its program implementation plan will include using an existing network of 34 weatherization assistance program providers (e.g., various community action entities) as well as awarding other contracts to cities with populations over 75,000. Under the program, subrecipients have 2 years to fully expend the weatherization funding. The Texas Department of Housing and Community Affairs noted that it intends to periodically assess progress and determine if unobligated funds need to be moved to high-performing entities.

More broadly, a particular challenge or difficulty cited by the executive and legislative branch officials we contacted in Texas is the need for more guidance from OMB and other applicable federal agencies.<sup>21</sup> Regarding quarterly recipient reports, for example, the officials said that there is a lack of clarity regarding whether all agencies in the state must submit reports to OMB or whether each state must submit a consolidated report.

<sup>21</sup>OMB issued initial guidance on February 18, 2009, and provided additional guidance on April 3, 2009. As presented in this appendix, the observations of Texas officials are based on OMB's initial guidance only.



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The officials also noted that it would be useful to have a reporting “template” that specifies the specific data fields or information to be reported. Furthermore, the officials commented that rather than simply being directed to a Web site, it would be helpful to have a centralized point of contact in Washington, D.C., for receiving and addressing questions. In April 2009, the Governor’s Office and State Comptroller of Public Accounts officials continued to express concerns to us about unclear guidance from federal agencies on allowable uses and reporting requirements. Also in April 2009, the officials informed us that the Office of the Governor had hired a consulting company, and six consultants had been staffed to track deadlines and work with state agencies to assist Texas in meeting Recovery Act reporting requirements.

Regarding other opportunities for enhancing Recovery Act funding accountability, the executive and legislative branch officials we contacted in Texas advocated that various oversight entities in the state be concurrently notified when funds are distributed. As mentioned previously, in Texas, the state-level decision-making process regarding use (and accountability and transparency) of federal Recovery Act funds involves several entities or key stakeholders, particularly the Office of the Governor, the Office of the Comptroller of Public Accounts, the State Auditor’s Office, and the Legislative Budget Board. Generally, in our meetings with representatives of these entities, a common theme expressed has been a desire to be notified by federal authorities when Recovery Act funds are distributed to Texas state agencies and/or localities. The representatives stated that concurrent notification to the state’s key stakeholders would help to further ensure accountability and transparency.

In April 2009, officials from the Office of the Governor and the State Comptroller’s Office told us that, in its disbursement of Recovery Act funds to the state, the federal government was not identifying these funds separately from other federal funds. The Texas officials cited increased FMAP funding as an example. Absent separate coding from the disbursing federal agency, the Texas officials said that the state relies on the Texas Health and Human Services Commission to inform the State Comptroller’s Office of what portion of the combined funds are Recovery funds. The Texas officials commented that it would be helpful if the federal government put in place the coding structure to identify Recovery Act funds separately from other federal funds—as they believe the Act requires—before Recovery Act funds are disbursed to Texas.

### Plans for Assessing the Impact of Recovery Act Funds Are Evolving

The executive and legislative branch officials we contacted in Texas—including officials from the Office of the Governor, the Office of the Comptroller of Public Accounts, the State Auditor's Office, the Legislative Budget Board, and various program agencies—recognized the importance of the state taking steps to assess the impact of Recovery Act funds in terms of preserving and creating jobs, assisting those individuals most impacted by the recession, and so forth. In late January 2009, for example, in preparing to implement the transportation components of the anticipated national economic recovery program, the Texas Transportation Commission recognized that a primary purpose of the recovery program is to “create and sustain jobs.”<sup>22</sup>

Texas officials commented that agencies in Texas—a state that has a performance-based budgeting process—already have performance measures in place for their respective programs and operations, although some Recovery Act-related adjustments or modifications may be needed. Texas Department of Transportation officials noted, for example, that contracts involving the use of Recovery Act funds will have special provisions requiring contractors to report on jobs created. These officials also cited potential difficulties in measuring the impact of Recovery Act funds used for programs that commingle these funds with other federal or state funds.

Finally, Texas officials told us that the Governor's Office has taken the lead in administering the state's responsibilities under the Recovery Act. As mentioned previously, the Governor's Office chairs a Stimulus Working Group with representatives from the state agencies that have a role under the Recovery Act. Texas officials were uncertain as to whether a specific agency would be designated to be responsible for compiling an overall assessment of the impact of Recovery Act funds in the state. The officials added, however, that the state's legislature was still in session and that the forthcoming biennial general appropriations bill—which will have a separate section specifically for Recovery Act funds—could perhaps assign such responsibility to an agency.

<sup>22</sup>Texas Transportation Commission, “Report on: Economic Recovery Plan,” presented at January 29, 2009, meeting by John Barton, Assistant Executive Director Engineering Operations.

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**Texas's Comments on  
This Summary**

We provided the Governor of Texas with a draft of this appendix on April 17, 2009. A Senior Advisor, designated as the state's point of contact for the Recovery Act, responded for the Governor on April 20, 2009. In general, the Senior Advisor agreed with the information in this appendix but wanted us to provide more context for the views of the State Auditor regarding potential areas of vulnerability with Recovery Act funds. We added contextual perspectives to address this concern and the Senior Advisor's belief that Texas is equipped to meet its responsibilities under the Recovery Act. The Senior Advisor also provided technical suggestions that we incorporated where appropriate.

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Acknowledgments**

In addition to the contacts named above, Danny Burton, Assistant Director; K. Eric Essig, auditor-in-charge; Yecenia Camarillo; Camille Chaires; Sharhonda Deloach; Michael O'Neill; Daniel Silva; Gabriele Tonsil; and Christy Tyson made major contributions to this report.

## Appendix XIX: Washington, D.C.

### Overview

**Use of funds:** An estimated 90 percent of Recovery Act funding provided to states and localities nationwide in fiscal year 2009 (through Sept. 30, 2009) will be for health, transportation, and education programs. The three largest programs in these categories are the Medicaid Federal Medical Assistance Percentage (FMAP) awards, highways, and the State Fiscal Stabilization Fund.

#### ✓ Medicaid Federal Medical Assistance Percentage (FMAP) Funds

- As of April 3, 2009, the Centers for Medicare and Medicaid Services (CMS) had made about \$87.8 million in increased FMAP grant awards to the District of Columbia.
- As of April 1, 2009, the District had drawn down about \$49.9 million, or about 57 percent of its initial increased FMAP grant awards.
- District officials plan to use funds made available as a result of the increased FMAP to cover an increased caseload, offset general fund deficits, and maintain current Medicaid eligibility and benefit levels.

#### ✓ Transportation—Highway Infrastructure Investment

- The District of Columbia was apportioned \$123.5 million for highway infrastructure investment on March 2, 2009, by the U.S. Department of Transportation.
- As of April 16, 2009, the U.S. Department of Transportation had obligated \$36.6 million for one project in the District of Columbia.
- The District of Columbia plans to use these funds for reviewed and vetted "shovel ready" projects, such as pavement restoration and resurfacing work on federal roadways, once the appropriate contracting processes have been completed.

#### ✓ U.S. Department of Education State Fiscal Stabilization Fund

- The District of Columbia was allocated \$89.4 million from the initial release of these funds on April 2, 2009, by the U.S. Department of Education. District officials intend to use these funds to increase aid across all schools in the District. As of April 2, 2009, about \$59.9 million of this allocation was available for the District to draw down upon.
- Before receiving the funds, states are required to submit an application that provides several assurances to the U.S. Department of Education. These include assurances that they will meet maintenance of effort requirements, or that they will be able to comply with waiver provisions, and that they will implement strategies to meet certain educational requirements, including increasing teacher effectiveness, addressing inequities in the distribution of highly qualified teachers, and improving the quality of state academic standards and assessments. As of April 15, 2009, the District was awaiting a response from the U.S. Department of Education on the District's proposed plan for using the funds before submitting an application.

In addition to the funding for these three programs, the District of Columbia is receiving Recovery Act funds under other programs, such as programs under Title I, Part A, of the Elementary and Secondary Education (ESEA), commonly known as the No Child Left Behind Act; programs under the Individuals with Disabilities Education Act (IDEA); and two programs of the U.S. Department of Agriculture—one for administration of the Temporary Food Assistance Program and one for competitive equipment grants targeted at low income districts from the National School Lunch Program. The District's plans for using these and other Recovery Act funds are discussed throughout this appendix.

**Safeguarding and transparency:** The District plans to use its existing financial systems to track the use of Recovery Act funds, and plans to use an ongoing accountability program to monitor District agency efforts to ensure that funds are used as intended. District officials are working to correct 89 material weaknesses in internal controls over both financial reporting and compliance with requirements applicable to major federal programs that were identified in the *Fiscal Year 2007 Single Audit Report* for the District of Columbia. The major federal programs in which these weaknesses were identified include programs that will be receiving Recovery Act funds, such as Medicaid's FMAP, ESEA Title I Education grants, and Workforce Investment Act programs. At present, it is not clear whether corrective actions will be completed before the Recovery Act funds are received by the District. This could increase the risk that Recovery Act funds may not be used properly. The District's Inspector General has also identified a number of District agencies with internal control and management issues that place them at risk for misusing Recovery Act funds. The District has initiated a Recovery Act Web site to help ensure that its Recovery Act efforts are transparent to the public.

**Assessing the effects of spending:** The District plans to assess the impact of Recovery Act funds by using the information in reports required by federal agencies under the Recovery Act, including information on the economic impact of the funds, such as on job creation. The District has provided initial guidance to city agencies on the tracking and use of Recovery Act funds and is awaiting further guidance from the federal government, particularly information related to measuring jobs. District officials stated that the Office of Management and Budget (OMB) should provide a common definition of "job" and a metric to measure the number of jobs that are created by Recovery Act funds. District officials are also concerned about the lack of guidance for the methodology of tracking the new jobs created.

### District of Columbia Beginning to Use Recovery Act Funds

The Mayor of the District of Columbia has established 13 work groups to oversee the use of Recovery Act funds in each program area. Each work group is led by the head of a District agency or department, or their designee, who reports to the City Administrator through his Recovery Act coordinator. The work groups will collaborate to make decisions on the use of Recovery Act funds. As of April 3, 2009, the District had been allocated about \$240 million in Recovery Act funds. The City Administrator stated that the District is committed to taking full advantage of the opportunities provided by the Recovery Act, and is committed to doing so in a manner that is fiscally responsible, efficient, effective, and transparent, while addressing the goals of the statute and the needs of District residents. The District has begun to use the Recovery Act funds as follows.

**Increased Federal Medical Assistance Percentage Funds:** Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The amount of federal assistance states receive for Medicaid service expenditures is known as the Federal Medical Assistance Percentage (FMAP). Across states, the FMAP may range from 50 to no more than 83 percent, with poorer states receiving a higher federal matching rate than wealthier states. The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>1</sup> On February 25, 2009, the Centers for Medicare & Medicaid Services (CMS) made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the enactment of the Recovery Act.<sup>2</sup> Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs; (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs; and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act are for state

<sup>1</sup>See Recovery Act, div. B, title V, § 5001.

<sup>2</sup>Although the Recovery Act was enacted on February 17, 2009, states generally may claim reimbursement for the increased FMAP for Medicaid service expenditures made on or after October 1, 2008.

expenditures for Medicaid services. However, the receipt of the increased FMAP may reduce the funds that states must use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.

As of April 1, 2009, the District of Columbia had drawn down \$49.9 million in increased FMAP grant awards, which was 56.8 percent of its awards to date.<sup>3</sup> District of Columbia officials reported that they plan to use funds made available as a result of the increased FMAP to cover an increased caseload, offset general fund deficits, and maintain current eligibility and benefit levels in the District's Medicaid program.

**Transportation—Highway Infrastructure Investment:** The Recovery Act provides additional funds for highway infrastructure investment using the rules and structure of the existing Federal-Aid Highway Surface Transportation Program, which apportions money to states to construct and maintain eligible highways and for other surface transportation projects. States must follow the requirements for the existing programs, and in addition, the governor or other appropriate chief executive must certify that the state or local government to which funds have been made available has completed all necessary legal reviews and determined that the projects are an appropriate use of taxpayer funds.

As of March 2, 2009, the District's Department of Transportation was apportioned \$123.5 million in Recovery Act funds for highway infrastructure and has identified "shovel ready" projects for these funds. According to the District of Columbia's certification, approximately \$56 million in projects have been fully reviewed and vetted. As of April 16, 2009, the U.S. Department of Transportation had obligated \$36.6 million for one District project—the demolition and reconstruction of the existing New York Avenue Bridge over the railroad.

**U.S. Department of Education State Fiscal Stabilization Fund:** The Recovery Act created a State Fiscal Stabilization Fund (SFSF) to be administered by the U.S. Department of Education (Education). The SFSF provides funds to states to help avoid reductions in education and other essential public services. The initial award of SFSF funding requires each state to submit an application to Education that assures, among other

<sup>3</sup>The District of Columbia received increased FMAP grant awards of \$87.8 million for the first three quarters of federal fiscal year 2009.

things, it will take actions to meet certain educational requirements, such as increasing teacher effectiveness and addressing inequities in the distribution of highly qualified teachers.

As of April 15, 2009, the District was awaiting a response from Education on the District's proposed plan for using the funds to increase funding for education on a per student basis. Once this response is received, the District will submit an application to the federal government and expects to receive about \$89.4 million in fiscal stabilization funds. The District is home to about 220 schools in 60 local education agencies (LEAs). The District's 60 LEAs include one large public school system (District of Columbia Public Schools, or DCPS) and 59 smaller LEAs that are mostly single public charter schools. For the 2008-2009 school year, about 64 percent of District students were enrolled in DCPS, while about 36 percent were in public charter schools. District officials stated that they intend to distribute stabilization funds across all 60 LEAs.

**Other Education Funds:** The District expects to receive about \$37 million in Recovery Act funds for its ESEA Title I program. Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA), as amended by the No Child Left Behind Act provides funds to LEAs for schools that have high concentrations of students from families living in poverty in order to help improve teaching and learning. District officials told us that it may be a challenge to disburse funds rapidly while also meeting programmatic requirements. They also told us they did not yet know how the LEAs were planning on using these funds.

The District also expects to receive about \$18.8 million in stimulus funds for Individuals with Disabilities Education Act (IDEA) programs. About \$16.4 million will be used for Part B grants to states, and about \$260,000 for Part B grants for preschool children. The other \$2.1 million will be used for Part C (state grants for infants and families). Officials told us that they were unsure of how IDEA funds would be used, but they anticipate being able to serve more children under each program, improve methods for assessing the performance of students with disabilities, and improve services to children and compliance with IDEA's requirements.

**Public Transit Capital Assistance:** The U.S. Department of Transportation, through the Federal Transit Administration (FTA), has apportioned funds for Transit Capital Assistance grants. Although these funds are not apportioned directly to the District, the Washington Metropolitan Area Transit Authority (WMATA), which serves the District of Columbia and the surrounding area, estimates that WMATA will receive



approximately \$202 million in Recovery Act funding from FTA. WMATA plans to use these funds for 29 projects, including improving information technology and operating systems, maintenance, repair and replacement of buses, and renovation of passenger facilities in disrepair. According to its Web site, WMATA expects to make its first Recovery Act purchase of 45 hybrid-electric buses at the end of April 2009.

**Workforce Investment Act (WIA):** As of April 3, 2009, the District's Department of Employment Services had been allocated about \$1.5 million for adult Workforce Investment Act (WIA) programs, about \$3.8 million for dislocated workers programs, and almost \$4 million for youth programs. The District plans to use these Recovery Act funds in accordance with the U.S. Department of Labor's Guidance Letter Number 14-08. This guidance states that it is the intent of the Recovery Act that WIA adult funds be used to provide the necessary services to substantially increase the number of adults to support their entry or reentry into the job market, and that WIA dislocated worker funds be used to provide the necessary services to dislocated workers to support their reentry into the recovering job market. The guidance also emphasizes Congress's interest in using WIA youth funds to create summer employment opportunities for youth.

The District has also developed a plan that includes an increase in weekly benefits for the unemployed and an expansion of city services to help those filing unemployment claims and looking for work. The new benefits for the unemployed include additional compensation in the form of a supplemental \$25 weekly benefit outlined in the Recovery Act. In addition, the District announced an extension for those who have exhausted their unemployment benefits and are actively seeking work. According to District officials, the Mayor plans to forward legislation to the D.C. City Council that will enable those who will exhaust their unemployment benefits by late spring to extend them until December 2009. Both the new supplemental compensation and the extension of benefits are 100 percent federally funded as part of the Recovery Act.

**Housing Programs:** The U.S. Department of Housing and Urban Development (HUD) allocated about \$11.6 million to the District of Columbia to provide additional gap financing to Low Income Housing Tax Credit (LIHTC) projects under the Taxpayer Credit Assistance Program (TCAP). District of Columbia Department of Housing and Community Development (DHCD) officials told us that they were waiting for the Internal Revenue Service (IRS) and HUD to issue guidance for TCAP and the LIHTC Exchange programs before releasing details on their plans for implementing the program. Regarding the LIHTC Exchange program,

DHCD officials said they have questions about how the program will be implemented and that the answers to their questions could require revisions to state qualified allocation plans and procedures. As a result, further guidance from IRS will be needed to understand whether DHCD would use the program and, if so, what management changes, if any, will be needed for its implementation. As required by the Recovery Act, HUD allocated about \$27 million to the District of Columbia Housing Authority (DCHA) for capital and management activities, including modernization and rehabilitation of public housing projects. DCHA officials told us that they planned to use the allocation to fund improvements at ongoing projects included in their 5-year construction plan.

**Homeland Security and Justice Programs:** District officials expect to receive an additional allocation of about \$11.7 million through the Department of Justice's Edward Byrne Memorial Justice Assistance Grant Formula Program, which nearly doubles the total amount of grant funding awarded by the District's Justice Grants Administration in the last fiscal year. The District plans to use these funds in several areas, including prisoner reentry, detention and incarceration diversion initiatives, and court diversion services for at-risk youth. The District plans to change its funding priority targets by phasing out small discrete grants and instead focus on awarding grants that invest in long-term projects. According to District officials, they have collaborated with local criminal justice stakeholders and community groups to identify funding priorities.

### The District Plans to Use Existing Systems to Track Recovery Act Funds

District officials plan to track Recovery Act funds using existing financial systems. According to District officials, the financial system already has the infrastructure to track, monitor, and report the source of funds distributed to recipients to ensure strict compliance with the requirements of the Recovery Act and to monitor the flow of Recovery Act funds from the federal government to District agencies. District officials plan to account for Recovery Act funds in a manner similar to the way they track and manage grant funds, using a unique four-digit code. Officials from the District's Office of the Chief Financial Officer told us that they had notified District agency officials of the need to closely monitor Recovery Act funds. The District has not provided guidance to recipients regarding the tracking and use of Recovery Act funds. The District will determine what guidance needs to be provided to recipients once the District receives guidance from OMB.

### District Web site Used to Promote Transparent Use of Recovery Act Funds

The District has developed a Recovery Act Web site ([www.recovery.dc.gov](http://www.recovery.dc.gov)) that is intended to allow the public to track Recovery Act efforts. The Web site contains information on the management process the District plans to use to oversee Recovery Act spending, and provides the public a way to track Recovery Act spending and get information on grants and contracts that are available. The Web site also offers the public a means to submit ideas and to identify any waste or fraud. Further, the Mayor's certification of the use of the funds is also posted on the Web site, as is the testimony of the City Administrator and the Chief Procurement Officer on Recovery Act efforts before the D.C. Council—the District's legislative body.

### District Plans for Ensuring that Adequate Safeguards and Internal Controls Are in Place

#### The District Plans to Use Existing Accountability Program for Recovery Funds

The District will continue to use CapStat, a performance-based accountability program designed to make the District government run more efficiently and to ensure accountability, effectiveness of internal controls, compliance with reporting requirements, and reliable reporting about uses of Recovery Act funds. The CapStat process takes the form of weekly accountability sessions where the Mayor and City Administrator bring into one room all the executives responsible for improving performance on an issue to examine performance data and explore ways to improve government services, as well as to make commitments for follow-up actions. Each District agency participates in the program. Agency directors prepare for a session by examining their agency's performance measures and analyzing how they can improve their results.

#### Single Audit Identified Many Weaknesses in District Internal Controls

The *Fiscal Year 2007 Single Audit Report* for the District of Columbia identified 89 material weaknesses in internal controls over both financial reporting and compliance with requirements applicable to major federal programs. There were three financial reporting material weaknesses related to (1) fraudulent activities involving the Office of Tax and Revenue, (2) management of the Medicaid program, and (3) systemic weaknesses in DCPS. The single audit report identified material

weaknesses in compliance with requirements applicable to major federal programs including Medicaid's FMAP, ESEA Title I Education grants, and Workforce Investment Act programs, all of which will be receiving Recovery Act funds. The findings were significant enough to result in a qualified opinion for that section of the report. In addition, Education designated the District as a high-risk grantee in April 2006 because of its poor management of federal grants. If the District continues to be designated as a high-risk grantee, Education could respond by taking several actions, such as discontinuing one or more federal grants made to the District or having a third party take control over the administration of federal grants. OCFO officials told us that they are in the process of working with the federal agencies to address these material weaknesses, but it is unlikely the corrective actions will be completed before the District programs with these weaknesses begin receiving Recovery Act funds. This could increase the risk that Recovery Act funds may not be used properly.

**District's Office of  
Inspector General Intends  
to Monitor Recovery Act  
Funds During Ongoing and  
Planned Work**

The District's Office of Inspector General (OIG) has not developed a specific plan to audit Recovery Act spending, but OIG officials believe that ongoing and planned reviews will cover programs that are going to receive much of the stimulus money. OIG officials said that they continuously audit these four areas that have internal control problems and management issues: Medicaid, D.C. Public Schools, grants management, and the vendor/contractor payment process. As a result, the OIG maintains a regular presence in the D.C. Department of Health, DCPS, the Office of the Chief Financial Officer (OCFO), and the Office of Procurement. However, according to OIG officials, the OIG does not have legal authority to audit the District's Public Charter Schools.<sup>4</sup> The OIG also performs an annual audit of the District's Highway Trust Fund (separate from the Federal Highway Trust Fund). The OIG also plans to use the District's Comprehensive Annual Financial Report (CAFR) Committee, which the OIG chairs, to monitor Recovery Act spending by District agencies. This committee, which oversees D.C.'s Comprehensive Annual Financial Report, is working with the mayor's office regarding how the Committee can assist in monitoring Recovery Act spending. The OIG noted that they

<sup>4</sup>All public charter schools in the District of Columbia are required to submit annual financial audits to the D.C. Public Charter School Board. The charter schools select an auditor from a list of best qualified auditors and who has been approved by the D.C. Chief Financial Officer and the Public Charter School Board.

did not receive any additional funds or resources to carry out specific Recovery Act reviews.

**Role of the D.C. Auditor for Recovery Act Accountability Is Limited Due to Legislative Directive and Resource Constraints**

The Office of the District of Columbia Auditor is the legislative auditor for the District. The office exists to support the District City Council in meeting its legislative oversight responsibilities and to help improve the performance and accountability of the District government. The Auditor has the authority to conduct audits on District funds, including those used by the D.C. Charter schools, but is not set up to provide comprehensive services regarding federal funds except in instances of D.C. Council requests and pre-existing mandates. The D.C. Auditor's main body of work is developed on a rotating basis, where the Auditor selects specific activities or accounts to review every 3 years, concentrating on financial accounting and reporting. According to the D.C. Auditor, due to limited resources, they only plan to conduct audits based on scheduled rotations and requests, and they have no plans to audit Recovery Act funds. If, however, a planned audit concerns a program receiving Recovery Act funds, then the Auditor may adjust audit plans accordingly.

**Plans to Assess Impact of Recovery Act Funds Have Not Yet Been Developed**

The District plans to assess the impact of Recovery Act funds by using the information in reports required by federal agencies under the Recovery Act, including information on the economic impact of the funds, such as on job creation. However, District officials told us that calculating the number of jobs created through Recovery Act funds may be difficult. Officials stated that OMB should provide a common definition of "job" and a metric to measure the number of jobs that are created by Recovery Act funds. They are also concerned about the lack of guidance for the methodology of tracking the new jobs. They recommended that OMB create a centralized recovery tracking system that provides consistency in measuring how funds have impacted each state. While the direct impact of Recovery Act funds may be measurable, District officials are unsure of methods to track indirect impact and how to separate the impact of Recovery Act funds and the impact from other federal funds in programs that receive both sources and use both sources in their program implementation. Without this guidance, the District believes it will have difficulty producing reports using quantitative measures related to using the Recovery Act funds. In addition, officials would like to have a standardized reporting template with addendums for each federal agency. This would clarify confusion for the District and states since a reporting template would reduce reporting burden, especially since the amount of funding per issue area varies from state to state. Officials request that

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Appendix XIX: Washington, D.C.

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OMB provide a template for the format and required information for Recovery Act Web sites as well.

District officials also plan to use the CapStat performance-based accountability program to examine the impact of the use of Recovery Act funds on District agencies and programs.

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**District of Columbia's  
Comments on This  
Appendix**

We provided the Office of the Mayor of the District of Columbia with a draft of this appendix on April 15, 2009. On April 17, 2009, the City Administrator's office provided technical suggestions on the appendix that were incorporated, as appropriate.

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**GAO Contacts**

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**Staff  
Acknowledgments**

In addition to the contacts named above, John Hansen, Assistant Director; Mark Tremba, analyst-in-charge; Maria Strudwick; Shawn Arbogast; Marisol Cruz; Nagla'a El-Hodiri; Sunny Chang; Nancy Glover; Justin Monroe; Ellen Phelps Ranen; and Melissa Schermerhorn made major contributions to this report.

## Appendix XX: GAO Contacts and Staff Acknowledgments

### GAO Contacts

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For issues related to Medicaid and FMAP: Dr. Marjorie Kanof, Managing Director for Health Care, (202) 512-7114 or [kanofm@gao.gov](mailto:kanofm@gao.gov)

For issues related to highways and other transportation programs: Katherine A. Siggerud Managing Director for Physical Infrastructure, (202) 512-2834 or [siggerudk@gao.gov](mailto:siggerudk@gao.gov)

### Acknowledgments

The names of GAO staff who served on the teams for the selected states and the District are listed at the end of each respective appendix. In addition, the following staff contributed to this report: Stanley J. Czerwinski, Denise Fantone, and Yvonne Jones (Directors); Thomas James, James McTigue, and Michelle Sager (Assistant Directors); and Allison Abrams, David Alexander, Peter Anderson, Thomas Beall, Joanna Berry, Sandra Beattie, Bonnie Beckett, Pedro Briones, Kimberly Brooks, Kay Brown, Marcia Buchanan, Ted Burik, Steven Cohen, Nancy Cosentino, Robert Cramer, Michael Derr, Kevin Dooley, Heather Dowey, Colin Fallon, Alice Feldesman, Andy Finkel, Shannon Finnegan, Jim Fuquay, Vicky Green, Brandon Haller, Anita Hamilton, Tracy Harris, Laura Heald, Michael Hrapsky, Mary Catherine Hult, Susan Irving, Shirley Jones, Stuart Kaufman, Karen Keegan, Martha Kelly, Ba Lin, Edward Leslie, Leslie Locke, Steve Martin, JoAnn Martinez, Kim McGatlin, John McGrail, Donna Miller, Sheila Miller, Clarita Mrena, Elizabeth Morrison, Andy O'Connell, Lisa Pearson, Janice Poling, Brenda Rabinowitz, Carl Ramirez, Mathew Scire, Thomas Short, Michael Springer, George Stalcup, Andrew Stephens, Hemi Tewarson, Patrick Tobo, Gabriele Tonsil, Cheri Truett, Susan Wallace, Lindsay Welter, Michelle Woods, and Carolyn Yocom.

*Response to Hearing Questions**"Follow the Money: State and Local Oversight of Stimulus Funding"*

April 23, 2009 Hearing

Committee on Homeland Security and Governmental Affairs

United States Senate

## Questions for Gene L. Dorado

Acting Comptroller General of the United States

U.S. Government Accountability Office

**Senator Lieberman:** How much money would it require to separately fund state and local auditors to oversee stimulus spending?

At this point, it is not possible to estimate the amount of any incremental audit costs to the states for Recovery Act programs. OMB is working on several options to respond to the need for early internal control reporting and an appropriate audit focus on Recovery Act programs. The range of options available would also have a range of costs, with some options potentially having a minimal impact on incremental impact on audit costs. Until the audit proposals are made more concrete, it is not possible to estimate the amount of any additional audit costs. It is also important to remember that audit costs are often included in the larger category of "management and administrative costs," which may also be impacted by Recovery Act programs. We will continue to work with OMB to review options being proposed to achieve accountability over Recovery Act programs.

**Senator Tester :** Does the American Recovery and Reinvestment Act of 2009<sup>1</sup> prohibit contractors from using Recovery Act funds to hire workers from outside of an area that is experiencing high levels of unemployment to work on projects that are located in such an area?

Based on our review of the American Recovery and Reinvestment Act of 2009 (Recovery Act), there is no prohibition on hiring workers from outside of an area experiencing high levels of unemployment to work on projects that are located in such an area. Some Recovery Act programs do require that precedence be given to areas with high levels of unemployment. For example, under the Highway Infrastructure Investment Program, in selecting projects for funding, priority is to be given to those projects that are projected for completion within a 3-year time frame, and are located in economically distressed areas. Areas that have an unemployment rate that is, for the most recent 24-month period for which data are available, at least 1 percent greater than the national average employment rate qualify for designation as an economically distressed area.<sup>2</sup> However, the Recovery Act does not prohibit a contractor from hiring workers from outside the economically distressed area in which the highway project is located.

<sup>1</sup> Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

<sup>2</sup> 42 U.S.C. § 3161(a)(2).





July 28, 2009

The Honorable Joseph I. Lieberman  
Chairman  
The Honorable Susan M. Collins  
Ranking Member  
Committee on Homeland Security and Governmental Affairs  
United States Senate  
The Honorable Michael F. Bennet  
United States Senate

Dear Mr. Chairman, Ranking Member Collins, and Senator Bennet:

On June 26, 2009, you requested that I respond to questions for the official record of the Committee hearing titled "Follow the Money: State and Local Oversight on Stimulus Funding," held on April 23, 2009. At that hearing, we released our report titled "Recovery Act: As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues is Essential" (GAO-09-580) and I testified (see GAO-09-631T for my statement). The questions, along with our responses, follow.

**Responding to Questions from Ranking Member Susan M. Collins and Senator Michael F. Bennet**

**1. Based on your review of the states' and localities' plans for spending and overseeing Recovery Act funds, what 'best practices' have you discovered that states and localities should follow in developing and implementing their plans?**

And

**2. Your testimony provides some examples of what states are doing to meet implementation and accountability requirements. From my understanding, your report will also profile what your selected states have done so far. What steps are being taken to ensure that there is a sharing of best practices as we move through this process of distributing and accounting for stimulus funds? Has OMB looked in to ways that can ensure everyone is being made aware of different approaches in use? Especially when it comes to new programs, I imagine that it would be helpful to get a sense of what others are doing to use funds effectively.**

The Office of Management of Budget (OMB) and several national associations—representing various levels of state government—have begun efforts to share best practices on developing and implementing plans for distributing and accounting for Recovery Act funds. For instance, to ensure the accurate accounting of Recovery Act funds, OMB issued guidance to federal agencies that Recovery Act funds are expected to be separately identified and tracked in financial systems whether administered directly by federal agencies, or by third-parties through contracts or grants.<sup>1</sup> As reported in both our April and July 2009 reports<sup>2</sup>, the selected states and the District are taking measures to separately track these funds. Our reports, which are available on our web site ([www.gao.gov/recovery/bimonthly](http://www.gao.gov/recovery/bimonthly)), highlighted approaches in the Recovery Act tracking mechanisms planned by the states.

In addition to providing guidance on the tracking of Recovery Act funds, OMB plans to host a series of webinars describing implementation procedures for recipient reports. The purpose of the webinars is to clarify outstanding questions Recovery Act prime recipients, sub-recipients, and the general public may have regarding OMB's guidance and to foster greater communication between the recipients and OMB. These webinars will include the discussion topics including an overview of OMB's guidance, reporting requirements, and issues related to the reporting of job creation estimates.

During the course of our work we have also identified other efforts national associations are taking to share best practices regarding the distribution and accounting for Recovery Act funds. These efforts include:

- **Recovery Act Teleconferences.** To ensure that states are meeting the reporting and accountability requirements of the Recovery Act, the National Association of State Auditors, Comptrollers, and Treasurers, National Governors Association, and the National Association of State Budget Officers facilitate weekly teleconferences that include representatives from OMB and GAO. Through this coordinated approach, state officials are able to communicate directly with federal government officials regarding issues related to the reporting and compliance aspects of the Recovery Act. Furthermore, these teleconferences provide a forum where recipients can obtain additional informal guidance from OMB as states work to develop and implement processes to ensure the funds are spent efficiently while maintaining appropriate internal controls and reporting mechanisms for recipients.
- **National Association of State Auditors, Comptrollers and Treasurers.** To facilitate information sharing regarding the implementation of the Recovery Act, NASACT is planning to hold a half-day roundtable discussion during the

<sup>1</sup> OMB Bulletin No. 09-02, *Budget Execution of the American Recovery and Reinvestment Act of 2009 Appropriations* (February 25, 2009); and OMB Bulletin No. M-09-21, *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009* (June 22, 2009).

<sup>2</sup> GAO, *Recovery Act: As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues Is Essential*, GAO-09-580 (Washington, D.C.: Apr. 23, 2009); and GAO, *Recovery Act: States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses*, GAO-09-829 (Washington, D.C.: Jul. 8, 2009).

2009 NASACT Annual Conference in August. Additionally, in conjunction with the Association of Government Accountants and the Association of Local Government Auditors, NASACT hosts a series of audio conferences addressing issues in government auditing and financial management. The most recent audio conference addressed the key issues surrounding the practical implementation of OMB requirements and administrative costs for activities relating to the Recovery Act. State and local officials learned about the requirements from the perspectives of federal officials representing OMB and the U.S. Department of Health and Human Services. Officials from Arizona and Colorado also shared their perspectives on the implementing of the Recovery Act.

- **National Conference of State Legislatures.** The National Conference of State Legislatures (NCSL) launched an electronic discussion board in which its members can discuss issues relating to implementation of the Recovery Act. According to NCSL, the intent of this service is to help address questions regarding the Act and to serve as a forum for exchanging ideas, insights and best practices.
- **Council of State Governments.** The Council of State Governments (CSG) launched its own Recovery Act website ([www.staterecovery.org](http://www.staterecovery.org)) to help states: 1) determine potential funding opportunities; and 2) share best practices by tracking how the executive, legislative, and judicial branches of state government are responding to and affected by the Recovery Act. CSG also recently issued a 50-state report analyzing how states plan to use the flexible funding portion of the State Fiscal Stabilization Fund.
- **National Association of Counties.** Through its *Leading in Tough Times: Recovery Act Information* webpage, the National Association of Counties provides its members with links to Recovery Act resources and publications.
- **National League of Cities.** In addition to providing its member cities with access to Recovery Act resources, the National League of Cities hosts an ongoing series of webinars regarding the implementation of the Recovery Act. Recent topics included the following: maximizing the value of Recovery Act funding, the Workforce Investment Act Summer Youth program, transportation programs, and energy efficiency and conservation block grants.

#### Responding to Additional Questions from Senator Michael F. Bennet

**3. In addition to stimulative spending, the American Recovery and Reinvestment Act provided for significant amounts of tax credits for businesses to invest in our economy. What is being done to track these incentives in terms of identifying their link to job creation and economic growth? Will OMB provide more information on how these incentives are being used and whether they are spurring economic growth?**

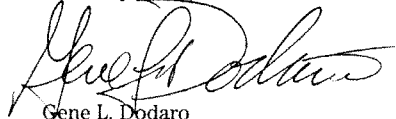
According to information in a May 2009 Council of Economic Advisers paper,<sup>3</sup> the administration does not plan to attempt to tie individual tax provisions in the Recovery Act to job creation and economic growth. Rather, the estimated total number of jobs created due to the combined spending, state fiscal relief, and tax provisions will be estimated based on a macroeconomic model that compares estimated numbers of jobs with and without the stimulus. The model incorporates various assumptions and data about the state of the economy. The administration plans to update its estimate of total jobs created as economic data are updated. In the future, economic researchers will likely undertake research that will attempt to refine and perhaps better estimate the effect of the Act on job creation and economic growth.

According to Department of the Treasury officials, the administration plans to publish information showing the estimated dollars flowing into the economy for certain Recovery Act tax provisions. These provisions include the making work pay and other individual credits and tax incentives for business. The estimates of dollars flowing into the economy will be based on the revenue losses for each provision that were estimated by the Department of the Treasury with assumptions made when the Act was being considered. The estimates will change if the economic assumptions underlying the 2010 budget change as new information becomes available.

In addition, for some tax provisions, the Internal Revenue Service (IRS) expects to report some data on usage. According to IRS information given to us, no later than October 10, 2009, IRS will begin public reporting on four benefits, including the first time homebuyer credit. IRS will likely have information on the number of returns filed claiming the credit before and after the Recovery Act, and on the extra dollars of credit taken beyond what the credit amounts would have been if only the 2008 credit had been in effect. According to IRS officials, the administration is continuing to consider what specific information it will be able to make available on the various Recovery Act tax provisions and when. We raised the need to collect this type of information in March 2009, and we will continue to monitor IRS's efforts to do this.

Thank you for the opportunity to participate in your April 23, 2009 hearing on the Recovery Act. Please contact me at (202) 512-5500, if you or other Committee members have additional questions.

Sincerely yours,



Gene L. Dodaro  
Acting Comptroller General  
of the United States

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<sup>3</sup> Executive Office of the President, Council of Economic Advisers, "Estimates of Job Creation from the American Recovery and Reinvestment Act of 2009," May 2009.

**Prepared Statement for Sen. Joseph Lieberman**  
**“Follow the Money:**  
**An Update on Stimulus Spending, Transparency, and Fraud Prevention”**  
**September 10, 2009**

Good morning and welcome to this fifth in a series of oversight hearings this Committee has called on the American Recovery and Reinvestment Act – the \$787 billion stimulus package we hope will help pull the economy out of the worst recession in the living memory of most Americans.

We hold this hearing on the heels of mixed news about an economy that is still not where we want and need it to be. After a slight decrease in the unemployment rate in July – down a tenth of a point to 9.4 percent – the jobless went back up to 9.7 percent in August – the worst rate in 26 years.

We know that unemployment is a lagging indicator of an economic recovery, so this was not entirely unexpected. We also know that, just a few months ago, our financial sector was on the verge of collapse, and the overall economy was teetering on the edge of another Great Depression.

Thankfully, both of those calamities have been averted. The stock market is up. Housing sales are up. And manufacturing grew last month for the first time in more than a year.

But the unemployment level now is above what many economists predicted when we passed the stimulus in February – particularly the numbers for the construction trades, where unemployment exceeds an astounding 17 percent in many states –20 percent in my home state of Connecticut.

Perhaps that explains why, when I met with workers in the construction trades in Connecticut last week, they were having a hard time feeling any positive effects of the stimulus.

The danger of a “jobless” recovery is all too real.

With that in mind, a lot of people, understandably, are asking if we could do more. Or can we implement what we have already passed faster – can we speed up the process so that more citizens feel the positive effects that we intended more quickly, while of course ensuring that taxpayer money is not wasted?

My answer is we must accelerate the pace of stimulus spending and tax cutting. So today we’re going to take a status check of what’s been done so far, and ask about the capabilities of all levels of government to administer Recovery Act programs as the pace of spending picks up this fall as planned.

It must be said that much has been accomplished since the Recovery Act was passed. While economists are never of one mind, most agree that the Recovery Act has helped halt the economic slide and is pointing us toward recovery.

And we need only listen to grateful governors and local officials to know that things would have been far worse without the Act's initiatives.

Here are some of the contributions to date:

- On the tax side, 95 percent of working Americans have seen their paychecks increase because of the Make Work Pay tax credit that has put about \$23.2 billion into the pockets of American families so far. And in total, more than \$62.5 billion has been pumped into the economy through tax relief under the Recovery Act, with \$225.5 billion still to come.
- Nearly 334,000 new homeowners have claimed the Recovery Act's \$8,000 First-Time Homebuyer Tax Credit and many analysts say this provision helped steady the housing market as we have seen new home sales increase for four months in a row.
- In transportation, over 6,700 highway projects have been approved and more than 2,200 are underway. Hundreds of airports across the country have been awarded funds for improvements, and about \$1.1 billion in Amtrak improvements are on the way.
- The Recovery Act is helping families through these tough times with extended Unemployment Insurance, increased Social Security Payments, more food stamp assistance and aid to states through increased Medicaid grants.
- Recovery Act payments to the states through the Federal Medical Assistance Percentage Program and the State Fiscal Stabilization Fund have helped states keep 135,000 teachers and 5,000 law enforcement officers on the job, allowing states and municipalities to avoid even more drastic cuts in services.

Besides the spending of stimulus money, another major topic of this hearing will be this Committee's continued interest in the transparency of Recovery Act spending. Since our last hearing, the Office of Management and Budget has released additional guidance regarding the extensive reporting required of recipients of Recovery Act funds. OMB has also given further direction on how recipients will report on jobs created or maintained by the Recovery Act.

But I don't think this guidance is enough to enable any interested American to burrow into the nitty-gritty details of spending on Recovery Act projects.

A final – but critical – challenge we want to deal with today is the federal government's efforts to prevent Americans from being bilked by scam artists who fraudulently promise government money in return for credit card information. Scams directly related to the stimulus appear to be few so far, but unfortunately tough economic times are always accompanied by scam artists who try to exploit people financially strapped and desperate for cash.

I welcome all our witnesses today and I look forward to your testimony.

**Prepared Statement of  
Senator Susan M. Collins**

**Follow the Money: An Update on Stimulus Spending, Transparency, and  
Fraud Prevention**

**September 10, 2009**

Seven months ago, the American Recovery and Reinvestment Act was signed into law. Since that time, this Committee has conducted oversight to help ensure that these funds are used as intended: to help revitalize the economy by creating needed jobs, improving roads and bridges, sustaining vital health care programs, and investing in infrastructure and science.

Today marks the fifth hearing that this Committee has held to review the use of Recovery Act funds. In these hearings, we have examined transparency initiatives such as the Recovery.gov website and the challenges facing state and local governments in accessing, using, and monitoring stimulus dollars.

These funds must be dispersed quickly to meet the goal of stimulating the economy, but we must ensure that haste does not make waste – or permit fraud or mismanagement. Striking the right balance between speed and caution has been a challenging task.

For example, we recently learned that the Social Security Administration erroneously sent about 10,000 stimulus checks for \$250 each to people who were either dead or incarcerated. This mistake may cost taxpayers about \$2.5 million and could have easily been prevented. Now, instead of these funds stimulating the economy, the Social Security Administration must work to recover them and put controls in place to prevent similar errors in the future.

Today, we will explore three issues that could blunt the economic recovery impact of the stimulus: unnecessary delay, inadequate transparency, and outright fraud.

First, some reports indicate that stimulus funds are entering the economy too slowly, delaying the potential economic benefits. OMB, however, has reported that it is on track to meet spending targets. I am interested in hearing our witnesses' views on whether spending to date has had the desired effect on the economy.

Second, I want to ensure that we are providing the American public with accurate and thorough information about stimulus projects around the country. Congress directed the creation of the Recovery.gov website to increase transparency – to allow the American public to monitor stimulus projects in their own states and report any abuses. Progress on Recovery.gov initially has been slow, however, particularly when compared to some private sector alternatives.

Third, I am concerned about the growing incidence of fraud and predatory scams that appear to be on the rise as con artists prey on citizens facing financial hardships. These crooks are smart and opportunistic. They exploit these tough economic times to lure Americans into scams that look and sound legitimate. They use phrases we hear on news reports and see in

headlines, such as “stimulus grants” and “government funding,” to confuse victims. They manufacture forms that have an “official” look to them, when in fact, the “services” offered are not connected to any government agency or to the Recovery Act.

To appreciate the potential that these scams have to grow and spread, possibly ensnaring thousands of trusting consumers, we must recognize that the federal stimulus program is instantly recognizable; it is a part of our economic and political vocabulary. It carries so much weight that police in Florida recently used the lure of economic stimulus checks to conduct a sting operation in which seventy-six people were arrested.

The Florida example demonstrates the attention-drawing power that the words “economic stimulus” can have on the public. It is critical that we aggressively pursue scam artists who brazenly use the federal stimulus program as a spring board for fraudulent or other unfair activities.

I have brought two examples of mailings, sent to my constituents in Maine, to illustrate my point. The first example, sent shortly after Congress passed the Recovery Act, is misleading because it resembles an official government form and can easily be mistaken for a legitimate government offer of help and assistance.

As you can see, the mailing is particularly confusing because it refers to the Stimulus Act and looks like an IRS form, even providing an identification number for the individual.

The second example is a letter that claims the constituent is pre-approved for the “Consumer Debt Initiative” because he “may be experiencing a financial hardship.” The letter implies that this initiative was established under the “Economic Stimulus Act of 2009.” In the letter, the alleged manager of the so-called “Credit Relief Division” of the Consumer Debt Initiative – all fictitious, but realistic-sounding titles – encourages the constituent to call and refer to the case number provided.

I look forward to hearing from Chairman Leibowitz on the Federal Trade Commission’s efforts to identify, publicize, and prosecute stimulus scams.

I also appreciate the work that the Department of Justice has been doing to train more than 10,000 federal, state, and local officials to monitor the contracting process for abuses such as collusion and bid-rigging. Officials and agencies at every level of government can play an important watchdog role.

With a combination of education and enforcement, we can help prevent exploitation and stop scams. At the same time, this hearing should serve as a warning to con artists that our government is on the lookout.

We will alert citizens.

We will expose scams.

And criminals will be prosecuted.

Preventing fraud in the execution of stimulus funding is a key element to the ultimate success of the Recovery Act.

I wish to thank all four distinguished witnesses for their assistance, and I welcome their testimony.



4. ID Number 0226		Loan Modification - Payment Reduction		Code 0226	
b. Company Phone Number (888) [REDACTED]		Property State ME			
[REDACTED]		Property Type RESIDENTIAL			
Columbia, MD 21045		Notice Type 009-S		Subject NOTIFICATION	
d. Addressee's Personal ID Number BNAGU2T0					
e. Property address and ZIP code [REDACTED] 541 Portland, ME 04101-541 [REDACTED]		RE: HR 5140 Economic Stimulus Act of 2008			
State ME	Modification PROGRAM	Issue:	Program Director		

Form **009-S** Payment Reduction Notification**2009****PAYMENT REDUCTION NOTIFICATION****STIMULUS ACT 2008**

PLEASE READ ENTIRE DOCUMENT CAREFULLY

RE: Payment Reduction Program

Issued Date: February 24, 2009

Your property located at [REDACTED] may be eligible for special modification program guidelines created in conjunction with the Governmental Economic Stimulus Act of 2008.

These new programs may enable you to modify your existing home loan and reduce your monthly mortgage payments, receive interest rate reductions, and /or freeze your existing interest rate, without the traditional restrictions on credit history, income or employment status, equity and reserves.

If you have experienced financial hardship, have late mortgage payments, or have negative equity Call 1-888-[REDACTED] to confirm eligibility. When calling please reference Reservation code BNAGU2T0

HR 5140 Economic Stimulus Act of 2008 was designed to provide economic stimulus through recovery rebates to individuals, incentive for business investment, and increase in conforming and loan limits. This Act became Public Law No: 110-185 on February 13, 2008 and will expire on 12/31/2008. HR 5140 information is available to anyone at [www.govtrack.us/congress/bills?bill=110-5140](http://www.govtrack.us/congress/bills?bill=110-5140)

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**PERSONAL & CONFIDENTIAL**

**Robert L. Nabors II**  
**Deputy Director of the Office of Management and Budget**  
**Testimony for the Senate Homeland Security and Governmental Affairs Committee**  
**September 10, 2009**

Chairman Lieberman, Ranking Member Collins, distinguished members of the Committee, thank you for inviting me to speak to you once again about the implementation of the American Recovery and Reinvestment Act. I would like to talk today about the progress that we have made since I last testified in April, and about the work that the Administration – and OMB in particular – is doing to make the implementation of the Recovery Act as efficient, effective, and transparent as possible.

**In order to understand where we are today, I think it is important to remember how bad things were when the Administration took office.**

In the fourth quarter of last year, real GDP was declining at a rate of almost 5.5 percent per year. In that quarter alone, household net worth fell by about \$5 trillion, dropping at a rate of 30 percent per year.

In terms of employment, the fourth quarter of last year saw a loss of 1.7 million jobs – the largest quarterly decline since the end of World War II and a number only to be exceeded in the first quarter of this year, when 2.1 million jobs were lost. Employment fell during every month of 2008.

This slowdown in economic activity created a pair of trillion-dollar deficits. One was the budget deficit, which had ballooned to \$1.3 trillion even before President Obama came in to office. The other was the deficit between what the economy could produce and what it was producing. This output gap amounts to about 7 percent of the economy.

When Congress passed the Recovery Act, we all knew that the economic situation was serious; many experts and commentators alike predicted that we were on the cusp of a second Great Depression. Indeed, the revised GDP statistics show that the actual decline in GDP growth in the third and fourth quarters of last year was about twice as large as the preliminary estimates we had at the time indicated. If we did nothing, it is conceivable that those dire predictions could have become true.

**Instead, the Recovery Act, along with other efforts to stabilize the financial and housing sectors, pulled us back from the brink and has begun to lay a new foundation for long-term economic growth.**

In the second quarter of the calendar year, the first full quarter since the enactment of the Recovery Act:

- GDP fell at a rate of one percent, a much slower rate than the previous two quarters, when it fell at a rate of six percent. Both Goldman Sachs and Mark Zandi of Moody's

Economy.com have estimated that GDP growth in the second quarter was given a significant boost due to the Recovery Act, suggesting that in its absence, the economy would have shrunk by three to four percent in the second quarter. These analysts also project an even more significant boost to the economy in the third quarter;

- State and local spending increased 2.4 percent, after falling for the last six months. This unexpected reversal linked directly to fiscal relief that has been provided to states through the Recovery Act;
- Household income grew at a yearly rate of almost five percent following declines in the previous nine months; and
- Business investment contracted much less than expected, as confidence is slowly returning to the economy.

The Recovery Act is also helping to slow the rate of job loss – perhaps the most significant effect of this recession.

Although the unemployment rate remains elevated at 9.7 percent, the economy is losing jobs at a slower pace – from 2 million jobs lost in the first quarter to 1.3 million jobs lost in the second quarter of 2009. Last Friday, the Bureau of Labor Statistics reported the loss of 216,000 jobs in August. This is 60,000 fewer jobs than were lost in July, and 525,000 fewer jobs than were lost in January 2009 – the month with the highest recorded job loss during this recession. This is far from a full recovery, but private forecasters are crediting the Recovery Act for staunching the job loss associated with the recession and thereby protecting hundreds of thousands of jobs. Analysts from Moody's to IHS Global Insight, to the Economic Policy Institute and others all estimate the Recovery Act has created or saved between 500,000 to 750,000 jobs – and some reputable economists say as many as a million. We also know anecdotally that jobs are being saved in critical areas like education, law enforcement, and construction. To give just a few examples that were highlighted in GAO's July report:

- New York City School district officials reported that, due to State Fiscal Stabilization Funding (SFSF) from the Recovery Act, they were able to retain approximately 14,000 jobs;
- The Richmond County School System in Georgia reported that it would be able to retain positions including teachers, paraprofessionals, nurses, media specialists and guidance counselors; and,
- California, Florida, North Carolina, and Massachusetts also reported that they would be able to retain positions thanks to SFSF funding, including teaching positions that would otherwise have been cut.

While many school districts continue to be squeezed as revenues shrink, the Recovery Act is making a real difference. As the Florida Governor has said, "[I]t's pretty incredible that 26,000 teachers will continue to be able to work for Florida's children because of these additional

moneys...and that's really the point: this is to help people, to help our education system, to help people with health care needs, and it's the people's money so they deserve it."

Make no mistake, the President is not satisfied – and will not be satisfied – until we are adding jobs to the economy again. But, as the Congressional Budget Office (CBO) recently noted, the severity of current unemployment reflects "a much sharper ongoing deterioration in underlying labor market conditions than had been anticipated, rather than a smaller impact of the [Recovery Act] legislation." CBO credits the Recovery Act as one of the reasons why economic activity is expected to begin its rebound in the second half of 2009.

**There is no doubt that the Recovery Act is moving significant resources into our struggling economy.**

As of April 3, the week I last testified before this Committee, our accounts showed that Federal agencies had obligated about \$54 billion. Today, nearly \$234 billion has been obligated. When combined with over \$66 billion in tax relief, that totals about \$300 billion that has been committed to date. As agencies have paid out nearly \$94 billion so far, up from about \$12 billion on April 3, the budgetary effects of the Recovery Act currently exceed \$159 billion. This pace of spending is consistent with our original goal of outlaying 70 percent of funds – or about \$551 billion – by the end of FY 2010, and is also consistent with CBO's initial projections of budgetary effects, as CBO notes in their recent report.

Notably, we are ahead of schedule on several key priorities. The Recovery Act set an ambitious benchmark that all States had to obligate at least 50 percent of their highway dollars in just 120 days. Every State not only met that goal, but exceeded it by at least 10 days. Key Department of Education programs are investing Recovery dollars several months ahead of schedule. The Making Work Pay tax credit was implemented about three months ahead of schedule. And GAO noted that Recovery Act funds are moving to states faster than anticipated.

Likewise, the Administration recently set and met a number of ambitious targets on Recovery Act implementation. At the beginning of the summer, the Vice President presented to the President a "Roadmap to Recovery," a plan for ten major projects that would help to define the Recovery Act during its second 100 days and speed implementation. The Roadmap set key targets for these projects to meet during the second 100 days. Last week, the Vice President announced that, thanks to agencies' hard work, we met or exceeded each of these targets. For example, the Administration committed to enabling 1,129 Health Centers in 50 states and eight Territories to provide expanded service to approximately 300,000 patients. The Department of Health and Human Services exceeded this goal, providing expanded services to about 500,000 patients.

**Through a variety of means, Recovery Act funds are making resources available to individuals and communities, and advancing critical projects at a time when funding is scarce.**

Tax relief accounts for more than a third of total Recovery Act funds. Already, 95 percent of Americans have seen an increase in their take-home pay thanks to Making Work Pay. Nearly 1.5

million people have claimed the First Time Homebuyers Tax Credit over the course of 2009, largely owing to the expanded version of the credit passed in the Recovery Act. We know that at least 334,000 taxpayers have claimed the Recovery Act credit to date – a number that is likely to increase once all tax filing season data is collected and analyzed.

About another third of funding is devoted to safety-net programs that provide immediate relief to the most vulnerable. Thanks to the Recovery Act, 54 million seniors, as well as veterans and other high-need groups, have received \$250 relief payments. Families qualifying for food assistance through the Supplemental Nutrition Assistance Program (SNAP) have seen their benefits increase by over 13 percent, and state governments have received over \$34 billion in additional Medicaid funds. Additionally, those facing job loss are collecting an extra \$25 a week in unemployment benefits – assistance that has already benefited over 12 million Americans.

Finally, about a third of Recovery Act funds are devoted to investments in discretionary programs that improve communities and invest in critical infrastructure. To date, over 30,000 Recovery Act projects – ranging from community health center expansions to military facility upgrades to transportation construction projects – have already been approved, and across the country, there are literally shovels in the ground. For example, more than \$28 billion has been obligated to fund over 10,000 shovel-ready transportation construction projects – over 4,600 of which are already underway.

Not only are projects like these being delivered on-time – and, in many cases, ahead of schedule – but under-budget. Department of Defense contracts are coming in about 12 percent under-budget, resulting in hundreds of millions of dollars in savings. Most GSA bids are coming in eight to ten percent below estimated costs. The Department of Homeland Security came in so far under-estimate on installation of in-line baggage handling systems at the nation's airports – \$243 million to be exact – that they were able to fund the systems at ten additional airports.

In addition, each of these projects is carefully reviewed by OMB to ensure that their uses of Recovery Act funds are thoughtful and appropriate. We regularly work with agencies to identify and revise projects that do not meet this threshold.

**We continue to work hard to ensure that Recovery Act funds are spent carefully and in a way that is transparent and accountable to the American people through Recovery.gov.**

OMB continues to play a significant role in upholding the accountability requirements mandated by the Recovery Act by issuing formal guidance; working with agencies, states, localities, and other stakeholders; and by taking extensive additional measures to prepare for the upcoming deadline on October 10 for recipients to submit detailed reports on how and where Recovery Act dollars are being used. The Act requires that by this date, direct recipients of funds report to agencies on the amount of funds received, information pertaining to projects or activities funded, and estimate the number of jobs created or retained.

To implement the recipient reporting requirements required by the Act, we have worked closely with the Recovery Board to develop and deploy [Federalreporting.gov](http://Federalreporting.gov), a web-enabled centralized reporting solution. After extensive testing, the website is up and running, and

available for recipient and agency registration. OMB's detailed guidance issued in June, informed by feedback from all stakeholders, defines the content of recipient reporting and the process by which they are submitted. Currently, we are supporting the Board's efforts to prepare to collect and process the data, which the Board will then make available to the public through Recovery.gov.

Per the requirements of the Recovery Act, the data in these reports will include project descriptions and information on the status of funds, job creation, and sub-recipient information. In addition to meeting the data elements required by the Act, OMB also responded to public input requesting an expansion of the reporting requirements on Recovery Act expenditures to capture payments to vendors, in addition to sub-recipients. We felt that it was within the spirit of the Recovery Act to do this, so we asked prime recipients (e.g., States) and sub-recipients (e.g., localities receiving awards from the States) to report on any vendors paid more than \$25,000 as dealers, distributors, merchants, or other providers of goods and services needed to conduct a Federal program. We worked closely with the Recovery Board to develop this additional requirement, and we listened to the Congressional and public input that we received. We believe that this additional requirement will provide a valuable tool for tracking federal grant dollars down to the local entities and their vendors – a level of visibility never before available.

As mandated by the Recovery Act, the October 10 reports will also require recipients to document the number of jobs that Recovery Act funds have enabled them to create or save. Putting people back to work is critical to our economic recovery, and this data will be essential for providing the transparency that the public needs to assess whether the Act is achieving its purpose. As there has been significant public uncertainty surrounding the methodology for counting jobs, our guidance provided funding recipients with two options. The preferred option is direct counting, and OMB strongly encourages prime recipients to make a direct employment count for each Recovery-funded project. However, we were mindful of the burden that this might place on some recipients, and realized that this could distract attention from critical recovery activities. So, the guidance offers prime recipients the option of extrapolating the jobs impact after collecting a set of verifiable project data. In the event that recipients choose to take advantage of this option, they are required to use methodologies that have been vetted and approved by the funding departments or agencies. Agencies were required to issue standard guidance on approved methodologies for jobs reporting. As of the end of August, 12 had done so – and four of these offered the option of using a statistical sampling methodology.

Without question, the October 10 deadline requires a lot of work from recipients, from Federal agencies, and from us – and we are taking proactive measures to provide support where we expect that it will be necessary. We continue to respond to concerns from the public and Congress by offering additional guidance and through frequently asked questions (FAQs). We are also collaborating with the Recovery Board to deploy on-site support teams to help manage the workload in State capitals and the localities that are likely to be dealing the highest volume of paperwork. They will provide state and local entities with government-to-government customer service that connects them to the Federal resources. For example, the support teams will have direct access to the Recovery Board's registrant database, which will allow them to see which recipients have or have not registered on Federalreporting.gov, and to walk recipients through the registration process if they are facing difficulties.

We have added capacity within OMB by establishing a new Recovery and Transparency Branch within the Office of Federal Financial Management. In addition to coordinating the work of the on-site liaisons with the Recovery Board, this branch works with states to address regarding OMB guidance on recipient reporting; coordinates response work of agency staff to assist states with recipient reporting; and interfaces with the Recovery Board and the Recovery Implementation Office on the full range of issues states face as they prepare for and conduct reporting.

We have tried our best to anticipate the needs that the October deadline will create, and we are committed to remaining responsive over the coming weeks and months. OMB, working with the Recovery Board and other Federal experts, has conducted seven webinars (more than 17,000 registrants participated, and the forms remain online as a resource) and a total of more than 20 different training sessions to explain the responsibilities of recipients of ARRA funding; discuss how to calculate and report Job Creation Estimates; and review the technical solutions and required data elements for reporting on ARRA funds. We communicate regularly with stakeholders like the National Governors' Association, the National Conference of State Legislatures, and groups representing State Auditors, Comptrollers, Treasurers, CIOs, and Budget and Procurement officers.

**This brings me to my final point, which is that we are committed to continuing active communication with stakeholders, including funding recipients and our partners in Recovery Act oversight, like all of you in who are in this room today. Together, we've made a lot of progress since April, but there is still a long road ahead as we perfect our oversight and implementation efforts to deliver on the President's promise of unprecedented transparency and accountability.**

Such communication is of the highest priority for OMB and for the Administration overall. Notably, the Vice President remains personally engaged in these efforts on a constant basis, holding weekly calls with governors and mayors. More than 100 mayors and county executives and all nearly all governors have participated in these calls.

In response to a recommendation from GAO, we have also taken increased measures to make sure that states are notified promptly of grants and contracts that are awarded within their jurisdiction. Our intent is for this increased level communication to facilitate a smoother process for states as they prepare for the reporting deadline.

Also in response to recommendations from GAO and this Committee, we have modified the OMB Circular A-133 Compliance Supplement such that the majority of programs with Recovery Act funding will be audited. We are also planning a pilot in which the auditors will accelerate their communications with management on identified internal control deficiencies to facilitate earlier corrective actions and better controls over Recovery Act funding.

We view Recovery Act implementation as a continuing conversation that has guided us at every stage and will continue to guide us as we identify and react to new challenges. We are committed to perfecting our data system and to taking the measures that are necessary to live up to the President's promise of transparency and accountability. And in doing so, we must always remember the big-picture – putting Americans back to work, increasing consumption and the demand for goods and services, and providing people with resources and services that will help them to weather difficult times.

I thank you, again, for this opportunity, and I look forward to answering any questions you might have.



**Prepared Statement of**  
**The Federal Trade Commission on**  
**Scams Related to the Economic Stimulus**

Chairman Lieberman, Ranking Member Collins, and members of the Committee, I am Jon Leibowitz, Chairman of the Federal Trade Commission ("Commission" or "FTC").<sup>1</sup> I appreciate the opportunity to appear before you today to describe the ways fraudulent marketers have used the economic stimulus program to bilk consumers. Like a cop on the beat, during these difficult economic times, the Commission is on the job, enforcing the law, and working with a heightened urgency. This testimony will highlight *Operation Short Change*, a law enforcement sweep the Commission announced on July 1st that targeted, and continues to target, entities defrauding American consumers hit by the economic downturn.

Job losses, foreclosures, and dwindling retirement accounts are forcing increasingly more Americans to search for ways to make ends meet. Opportunistic fraudsters have quickly adapted their schemes and sales pitches to take advantage of consumers during the economic downturn, with some capitalizing on the economic stimulus package. Using come-ons that offer the lure of free government grant money, these and other schemes have defrauded tens of thousands of consumers out of millions of dollars, and have been the focus of the Commission's ongoing law enforcement program<sup>2</sup> and consumer outreach efforts. Most recently, the Commission

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<sup>1</sup> The views expressed in this statement represent the views of the Commission. My oral presentation and responses to questions are my own and do not necessarily reflect the views of the Commission or any individual Commissioner.

<sup>2</sup> The FTC has broad law enforcement responsibilities under the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. 41, *et seq.* The statute provides the agency with jurisdiction over most economic sectors. Certain entities or activities, however, such as banks, companies engaged in common carrier activity, and companies engaged in the business of insurance, are wholly or partly exempt from FTC jurisdiction. In addition to the FTC Act, the agency has enforcement responsibilities under more than 50 other statutes and more than 30 rules governing specific industries and practices.

announced *Operation Short Change*,<sup>3</sup> a law enforcement sweep targeting fraudulent schemes designed to profit from the economic downturn. Together with fourteen state partners, the Department of Justice, and other agencies prosecuting criminal law violations, the Commission announced more than 120 law enforcement actions. *Operation Short Change* is one of a series of recent FTC fraud sweeps brought with our law enforcement partners: together, we have brought 389 legal actions in four sweeps in the last six months. These sweeps demonstrate the tremendous value of cooperation between the FTC and other federal and state partners.

Today's testimony highlights the agency's current experience with and efforts to combat fraud exploiting the economic stimulus program and other fraudulent schemes preying on financially-distressed consumers. The testimony also describes the tools the Commission uses to further its critical consumer protection mission.

#### **I. Financial Distress Fraud**

This past February, in the face of troubling economic times, Congress passed and the President signed the American Recovery and Reinvestment Act of 2009, an economic stimulus package that was widely reported as injecting \$787 billion into the economy. Con artists were quick to adapt their schemes, exploiting the news stories to target financially distressed consumers.

Prominent among these are scams promoting free government grants. *Operation Short Change* targeted these fraudulent schemes and those just one or two steps removed – scams that use the economic downturn to prey on financially distressed Americans. The Commission's

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<sup>3</sup> Press Release, Federal Trade Commission, *FTC Cracks Down on Scammers Trying to Take Advantage of the Economic Downturn* (July 1, 2009), available at <http://www.ftc.gov/opa/2009/07/shortchange.shtm>.

recently filed cases fall into four broad categories of familiar fraud: (1) government grant scams, (2) job placement scams, (3) phony income-generating opportunities, and (4) credit-related scams. This testimony focuses on government grant-related scams, with an overview of other cases the Commission has recently brought. The Commission's program to combat these types of fraud centers around its enforcement of Section 5 of the Federal Trade Commission Act ("FTC Act"), which prohibits unfair or deceptive acts or practices affecting commerce.<sup>4</sup>

#### **A. Government Grant Scams**

Con artists have sought to exploit the American Recovery and Reinvestment Act of 2009 by selling purported access to or expertise in obtaining free government grants. The FTC searched the Internet to identify those websites promoting ways to obtain a piece of the economic stimulus, and in March 2009, held a press conference to warn consumers to beware of such scams.<sup>5</sup> The event was highly successful at generating media that reached consumers, as the story was picked up by national and regional media outlets. The FTC warned specifically of websites promising government grant money to start a business, take a vacation, or just pay bills. Typical of hucksters chasing consumer dollars, some websites even used the image of President Obama and Vice President Biden to add legitimacy to their misrepresentations. Many of these schemes require consumers to pay substantial amounts of money in a fruitless attempt to obtain a much larger grant. Others simply ask consumers to provide personal information or send a very small payment to get information on how to get free government grant money. The scammers'

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<sup>4</sup> 15 U.S.C. § 45(a).

<sup>5</sup> Press Release, Federal Trade Commission, FTC Warns Consumers About Economic Stimulus Scams (March 4, 2009), <http://www.ftc.gov/opa/2009/03/stimulus scam.shtm>.

goal is to obtain consumers' financial account information, which they often use to run up additional charges. The Commission alerted consumers that whatever a website may say, the federal government does not award grants to individuals to pay personal expenses or bills, and the official source for information on available federal government grants is at [www.grants.gov](http://www.grants.gov), a free website operated by the U.S. Department of Health and Human Services.

As part of the Commission's efforts, it reached out to industry for help in pulling down ads for such scams. At the agency's request, major online ad networks have agreed to screen out ads touting the economic stimulus as providing grant opportunities for individual consumers. For instance, after being contacted about this problem, Facebook voluntarily pulled off the offending ads. The Commission wants to commend these networks for their help. The Commission also issued an alert to consumers to beware of scams relating to the economic stimulus package, stating particularly that the promise of stimulus money in return for a fee or financial information is always a scam.

The Commission initiated several recent law enforcement actions against government grant scams that explicitly and implicitly used the economic stimulus to bilk consumers out of money in order to get "free government grant money." Just last week, some of the defendants allegedly responsible for the "Grant Writers Institute" grant scam agreed to a preliminary injunction halting their operation pending final resolution of the matter by the court. On July 24th, at the request of the FTC and the Attorneys General of Kansas, Minnesota, and North Carolina, a federal district court had entered a temporary restraining order shutting down Grant

Writers Institute, its related entities, and its principals ("GWI").<sup>6</sup> The complaint charged that GWI falsely claimed that consumers were eligible for grants as part of the recently announced economic stimulus package. For example, consumers who called GWI in response to a mass-mailed postcard heard a recording that said, "If you've been reading the papers you know that recently our government released \$700 billion into the private sector. What you probably don't know is that there is another \$300 billion that must be given away this year to people just like you." The recording continued, "And if you're one of the lucky few who knows how to find and apply for these grants, you will receive a check for \$25,000 or more, and we guarantee it . . . If you don't get a check for \$25,000 or more, you pay nothing."

GWI telemarketers routinely represented to consumers that they were guaranteed a \$25,000 grant from the U.S. Government, and initially pitched a \$59 book titled "Professional Grant Writer 'The Definitive Guide to Grant Writing Success.'" GWI and its North Carolina-based telemarketers, who also were named as defendants in the complaint, then called consumers who had bought the book, convincing many to pay hundreds of dollars or more for grant research, writing, or coaching services by falsely claiming a 70 percent success rate in securing grant funding. In reality, few, if any, consumers ever received any grant money.

Other scams wave the promise of free government grant money as a lure to obtain consumers' financial account information and initiate recurring charges. Just two weeks ago, a U.S. district court shut down several Web sites that scammers allegedly had been using to falsely claim that they could help consumers get free government grant money, and a preliminary

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<sup>6</sup> *FTC v. Affiliate Strategies, Inc., et al.*, No. 5:09-CV-04104-JAR-KGS (D. Kan. July 24, 2009) (temporary restraining order).

injunction hearing relating to the other defendants is scheduled for September 11. On July 27, 2009, the Commission had filed suit against Grant Connect, LLC, its related entities, and its principals ("Grant Connect"), whose websites and employees misrepresented the likelihood that consumers would get grants and/or free money using the services of Grant Connect.<sup>7</sup> One of these websites displayed pictures of President Obama and Vice President Biden and proclaimed, "CHANGE Is Here! \$15 Billion in FREE Government MONEY for you." In addition to misrepresenting the availability of grants, as well as their expertise and success in obtaining government grants for consumers, the Commission charged that the defendants made unauthorized charges and debits to consumers' accounts for undisclosed monthly memberships by deliberately obscuring key terms and conditions in dense language and buried hyperlinks.

In a similar case filed June 23rd, the Commission alleged that website operators using names like Grants for You Now<sup>8</sup> represented that consumers who purchased their product would be likely to receive a government grant. The website, ornamented with the image of a suitcase bursting with money and boldly identifying specific federal government grants for housing and education, proclaims that "anyone who needs money for" paying off debt, home repair, and personal expenses can "benefit." Instead, the complaint charges, consumers who purchased the defendants' software program unwittingly enrolled in a negative option continuity program, subjecting them to recurring monthly charges of nearly \$100.

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<sup>7</sup> *FTC v. Grant Connect, LLC, et al.*, No. 2:09-CV-01349-RLH-RJJ (D. Nev. July 27, 2009) (complaint).

<sup>8</sup> *FTC v. In Deep Services, Inc.*, No. EDCV-09-1193-SGL (PGWx) (June 23, 2009) (complaint).

After a painstaking investigation that was part of Operation Short Change, on June 25th the Commission alleged that an individual operating as “Cash Grant Institute”<sup>9</sup> placed robocalls containing prerecorded messages to consumers throughout the United States, advertising “free grant money available from federal, state and local governments.” The complaint describes the numerous techniques defendants allegedly used to create a false aura of legitimacy, such as placing pre-recorded calls purportedly coming from the Cash Grant Institute in Washington, D.C., a website that includes images of President Obama and the U.S. Capitol building, and brazenly advertising a website as the “source of free money from the government.”<sup>10</sup> The Commission charged that the defendants did not provide grants; instead, they just redirected consumers to other websites purportedly providing grant-related services. In each of these cases, the Commission acted aggressively to put an immediate end to the alleged fraud, seeking and obtaining temporary restraining orders from federal district courts.<sup>11</sup>

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<sup>9</sup> *FTC v. Paul Navestad*, No. 09-CV-6329T (W.D.N.Y. June 25, 2009) (complaint).

<sup>10</sup> Another pending case alleging fraud in the promotion of government grants illustrates how hucksters attempt to falsify trust relationships to convince consumers to divulge their financial account information. In *FTC v. NHS Systems, Inc.*, No. 08-CV-2215 (E.D. Pa. May 15, 2008), the Commission alleged that defendants’ telemarketers led consumers to believe they were calling from U.S. government agencies and promised consumers that they were selected to receive grants or tax refunds that would never have to be repaid. In fact, the Commission charged, the telemarketers’ come-ons were simply a ruse to obtain consumers’ financial account numbers and to initiate hundreds of dollars in unauthorized charges to their accounts. The Commission moved aggressively to bring this scheme to a halt, obtaining a temporary restraining order and preliminary injunction from a federal district court.

<sup>11</sup> When the Commission discovers an entity is engaged in outright fraud – whether perpetrated through telemarketing or cloaked as a business opportunity – it uses aggressive law enforcement tools to bring the perpetrators to justice. After assembling a case against a suspected fraud, the Commission often applies to a federal district court for an *ex parte* temporary restraining order to halt the deceptive conduct and an asset freeze to preserve the possibility of returning money to consumer victims. Indeed, in many of the telemarketing and

### B. Other Economic Distress Frauds

In a time of economic distress with many Americans out of work, con artists see the opportunity to take advantage of those seeking simply to earn an honest day's wage.

Recognizing that out of work Americans can least afford to fall victim to scams, the Commission aggressively pursues employment scams.<sup>12</sup> As part of *Operation Short Change*, the Commission charged two schemes that targeted consumers who were searching for jobs. In its case against Career Hotline, the Commission charged that the defendants falsely "guaranteed" to obtain jobs for consumers in exchange for a fee ranging from \$89 to \$195.<sup>13</sup> Similarly, the Commission's complaint against Wagner Borges Ramos, operating as Job Safety USA, alleges that the defendant told job seekers that the only thing standing between them and a new job making

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business opportunity cases the Commission has brought, such as those described herein, staff has sought and federal courts have entered temporary restraining orders or preliminary injunctions.

Even after cases result in the successful entry of permanent injunctions against defendants, the Commission continues to monitor defendants' compliance with court orders, and brings actions against defendants who are in contempt. For instance, in *FTC v. Vocational Guides*, No. 3:01-CV-00170 (M.D. Tenn. April 6, 2009), the Commission obtained an order of contempt against defendant Timothy Jackson for his role in operating Grant Information Services, a government grant scam that misrepresented to consumers the availability of federal government grants to pay for personal needs. The defendant, who originally was under order for his involvement in a postal job scam, was permanently banned from all telemarketing and found jointly and severally liable for over \$7.6 million in consumer injury.

<sup>12</sup> The Commission has actively pursued cases against fraudsters who falsely represented that they were affiliated with or endorsed by the U.S. Postal Service, and that postal jobs were available in areas where their ads appeared. In one recent case filed against U.S. Work Alliance, the Commission charged a nationwide marketing operation with allegedly violating federal law by deceiving consumers into buying \$120 to \$140 worth of materials they thought would help them get federal postal jobs. *FTC v. U.S. Work Alliance, Inc.*, No. 08-CV-2053-WSD (N.D. Ga. June 19, 2008) (complaint).

<sup>13</sup> *FTC v. Career Hotline, Inc.*, No. 09-CV-1483-T17 (M.D. Fla. Aug. 4, 2009) (complaint).



“\$11-\$15/hour + benefits” was a five-digit “certificate registration number” or “CRN.”<sup>14</sup> In truth, the CRN was a ruse used by Borges, allegedly to trick consumers to pay him \$98 for a worthless credential for jobs that did not materialize. The Commission sought and obtained *ex parte* temporary restraining orders with asset freezes against both schemes.

The economic downturn has presented other opportunities for scammers seeking to capitalize on the misfortune of those who have seen their jobs disappear or their incomes slide. For example, as part of *Operation Short Change*, the FTC sued John Beck/Mentoring of America and Freedom Foreclosure Prevention Services, two fraudulent schemes using the home foreclosure crisis as fodder for their scams. The Commission charged that the defendants in John Beck/Mentoring of America marketed three get-rich-quick schemes, including how to buy and sell foreclosed real estate, and upsold coaching services for each of them. They allegedly made false and unsubstantiated claims about potential earnings for the users of the systems, duping hundreds of thousands of consumers into paying approximately \$300 million since 2004.<sup>15</sup> In the complaint filed against Arizona-based Freedom Foreclosure Prevention Services, LLC (“Freedom Foreclosure”), the Commission alleged that the defendants falsely claimed that business opportunity purchasers – after paying a fee of approximately \$1,500 – could easily earn \$10,000 per month by simply referring homeowners for Freedom Foreclosure’s loss mitigation services. In fact, the Commission charged, homeowners who turned to Freedom Foreclosure for help routinely lost their homes to foreclosures, and none of Freedom Foreclosure’s 2,500

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<sup>14</sup> *FTC v. Wagner Borges Ramos*, No. PJM 09-CV-1634 (D. Md. June 22, 2009) (complaint).

<sup>15</sup> *FTC v. John Beck Amazing Profits, LLC*, No. 09-CV-4719 (C.D. Cal. June 30, 2009) (complaint).

consultants earned the income they were promised for purportedly “helping” consumers out of foreclosure.<sup>16</sup> Other investment scams, such as the one the Commission alleged against an entity using the name Google Money Tree, simply lure consumers into divulging their financial account information using the false promise of a lucrative work-at-home opportunity.<sup>17</sup> Consumers who purchased the Google Money Tree work-at-home kit expected a small charge of \$1.99, but what they got were months of recurring monthly charges they never authorized.

With the tightening of credit in the marketplace, sellers of advance-fee credit cards and debt relief services are also aggressively targeting consumers. As part of *Operation Short Change*, the Commission sued a network of companies, charging that the enterprise tricked consumers into paying hundreds of dollars for credit cards that could only be used to purchase goods from a limited number of online catalog websites.<sup>18</sup> Similarly, the Commission has focused on sellers of debt relief services. For instance, this past June, the Commission sued Mutual Consolidated Savings,<sup>19</sup> a company that allegedly used robocalls to deceptively telemarket a supposed “rapid debt reduction” program that promised to reduce consumers’ credit card interest rates and save them money, but only drove them deeper into debt. In each of these

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<sup>16</sup> *FTC v. Freedom Foreclosure Prevention Services, LLC*, No. 09-CV-1167-PHX-PJM (D. Ariz. June 1, 2009) (complaint).

<sup>17</sup> *FTC v. Infusion Media, Inc.*, No. 2:09-CV-01112-RCJ (D. Ariz. June 22, 2009) (complaint).

<sup>18</sup> *FTC v. Group One Networks, Inc.*, No. 8:09-CV-0352-T-26-MAP (M.D. Fla. Feb. 25, 2009) (complaint).

<sup>19</sup> *FTC v. MCS Programs, LLC*, No. C09-5380RBL (W.D. Wash. June 25, 2009) (complaint).

cases, the Commission moved aggressively to halt the ongoing fraud by obtaining temporary restraining orders with asset freezes from federal courts around the country.

## II. Law Enforcement Tools

### A. Consumer and Business Education

In addition to the Commission's law enforcement activities, the agency reaches out to consumers to give them the tools they need to recognize and avoid fraud. In response to the recent economic downturn, the FTC developed several initiatives to help people manage their financial resources, avoid fraud, and be aware of emerging scams.

Because the announcement of a coordinated law enforcement sweep like *Operation Short Change* generates a great deal of attention from local and national media outlets, the Commission often uses sweep announcements to launch new consumer education campaigns and initiatives. For example, using *Operation Short Change* as a springboard, the Commission developed and released a video to educate the public on business opportunity fraud.<sup>20</sup> The video features a former con artist, Jim Vitale, describing the tools of the trade, including the techniques he used to rush consumers into sending their money. It provides a sobering glimpse into the lives of two individuals who lost money in business opportunity scams, and it gives consumers concrete advice on what they should do before investing in a business opportunity. As a result of significant coverage from national and local media outlets, the Commission's consumer protection message reached more than 35 million Americans.<sup>21</sup>

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<sup>20</sup> Available at <http://www.ftc.gov/multimedia/video/scam-watch/fraud-inside-look.shtm>.

<sup>21</sup> More than 160 stories about *Operation Short Change* aired on news stations across the country, and articles appeared in more than 30 print and online media sources.

Similarly, in conjunction with a federal-state crackdown on mortgage foreclosure rescue scam operators, the FTC produced a toolbox of mortgage-related resources for homeowners in distress; they are featured on a new web page at [www.ftc.gov/MoneyMatters](http://www.ftc.gov/MoneyMatters). Indeed, groups including NeighborWorks America, and the Homeowners Preservation Foundation – a nonprofit member of the HOPE NOW Alliance of mortgage industry members and U.S. Department of Housing and Urban Development-certified counseling agencies – are distributing FTC materials directly to homeowners at borrower events across the country, on their websites, in their statements, and even on the phone: when people call the nation's major mortgage servicers, they hear about the tell-tale signs of a mortgage foreclosure scam while they are on hold. Next month, the agency will distribute to thousands of community organizations, HUD certified housing counselors, and state attorneys general across the nation copies of a new video featuring the stories of real people who are working with legitimate counselors to save their homes from foreclosure.

The agency has focused outreach efforts on a number of other issues faced by people in economic distress, including stimulus scams, rental scams, church “opportunity” scams, offers for bogus auto warranties, and solicitations for phony charities that play on the public's concern for the welfare of our military troops and public safety personnel, especially at a time when budgets are shrinking.

Finally, in an effort to stem the number of false or misleading claims that consumers see, the agency has a publication for publishers and broadcasters to alert them to the kinds of claims – extravagant earnings promises, for example – that can signal a rip-off. The Commission also offers sample public service announcements that newspapers can run in the business opportunity

section of their classified section to remind readers to do their homework before buying a business opportunity.

#### **B. Policy and Research Initiatives**

To complement its law enforcement and educational initiatives, the Commission regularly conducts research to stay abreast of marketplace developments, and ensure the agency is best situated to prevent, deter, and halt consumer fraud. Toward these ends, the Commission has conducted two consumer fraud surveys, in 2003 and 2005, seeking to quantify fraud in the United States, and will continue to conduct research in 2010.<sup>22</sup>

More recently, to examine consumer fraud in depth, the Federal Trade Commission staff held a two-day Fraud Forum on February 25 and 26, 2009. In addition to federal, state and international law enforcers, staff invited consumer advocates, business representatives, criminologists and sociologists, all of whom share a keen interest in understanding fraud, and identifying ways to more effectively protect consumers from fraudulent schemes.<sup>23</sup> The purposes of the Forum were both to gain a greater understanding of fraud and the ways that fraud artists ply their trades, and to harness the collective knowledge and experience of Forum participants to advance anti-fraud initiatives.

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<sup>22</sup> Reports of the results of those two surveys, "Consumer Fraud in the United States: An FTC Survey, FTC Staff Report," (Aug 2004) ("2003 Survey") and "Consumer Fraud in the United States: The Second FTC Survey, FTC Staff Report," (Oct 2007) ("2005 Survey") are available at <http://www2.ftc.gov/reports/consumerfraud/040805confraudrpt.pdf> and <http://www2.ftc.gov/opa/2007/10/fraud.pdf>, respectively.

<sup>23</sup> Panelists and presenters at the Fraud Forum included 20 representatives from 16 federal, state, and international law enforcement or consumer protection agencies.

The Forum focused on the dynamics of fraud, including common traits of fraudsters and characteristics of victims in order to develop better methods of deterrence and prevention. As a reminder to law enforcement of the threat posed by the economic downturn, Jim Vitale, a former con artist who participated in the forum, aptly noted: "I'd have to say that the potential for business opportunity fraud is greater now than it would be in a booming economy . . . If the right marketing is done, it's [the] perfect storm."<sup>24</sup>

### III. Conclusion

The economic downturn and the stimulus package have shown how quickly and easily fraudsters adopt schemes to take advantage of individuals in financial distress. The Commission is committed to using its law enforcement authority aggressively to bring these schemes to a halt, and to continue deploying public alerts and educational materials to help consumers avoid being victimized in the first instance.

Thank you for providing the Commission with the opportunity to appear before the Committee to describe its efforts in this critical area.

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<sup>24</sup> Federal Trade Commission, Fraud Forum, *Panel 1: Becoming a Scam Artist, Understanding the Victim: Exploring the Psychology of Scammers and Victims*, at 45-46 (February 25-26, 2009), transcript available at [http://htc-01.media.globix.net/COMP008760MOD1/fic\\_web/transcripts/022509\\_sess1.pdf](http://htc-01.media.globix.net/COMP008760MOD1/fic_web/transcripts/022509_sess1.pdf).

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	G.F. Institute Kansas City Kansas "Your Access to Government Funds"	
	IMPORTANT RELEASE OF GOVERNMENT FUNDS PENDING	
To: John A Samples      Release Code: 9999 Deadline for response: 36 hours from receipt		
<p>Message:</p> <p>Our office is attempting to reach you &lt;stop&gt;. Urgent matter regarding upcoming release of Government Funds &lt;stop&gt;. Estimate of funds pending: \$25,000.00 (Twenty-Five Thousand Dollars) &lt;stop&gt;.</p> <p>Funds may be used at your discretion (bill payment, travel, continuing or advanced education, healthcare) &lt;stop&gt;.</p> <p>IMMEDIATE ACTION: To confirm your interest in these funds, please call number below &lt;stop&gt;. This is a TOLL-FREE CALL &lt;stop&gt;. You do not pay for this call &lt;stop&gt;.</p>		
<p>CALL THIS NUMBER TO VERIFY YOUR INTEREST IN \$25,000.00</p> <p><b>1-866-576-9176</b></p> <p>PLEASE QUOTE RELEASE CODE ABOVE.</p>		
A 1001 0000001		

TESTIMONY OF THE HONORABLE EARL E. DEVANEY  
CHAIRMAN, RECOVERY ACCOUNTABILITY AND TRANSPARENCY BOARD  
BEFORE THE COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL  
AFFAIRS  
UNITED STATES SENATE  
SEPTEMBER 10, 2009

Mr. Chairman and members of the Committee, I want to thank you for the opportunity to appear before you today to provide an update on the recent and planned activities of the Recovery Accountability and Transparency Board (the Board). My testimony today will address the current status and future direction of the Board's missions, and after my opening remarks, I will be glad to answer any questions you have for me.

I would like to begin by addressing some of the suggestions put forward by this Committee when I testified before you in April. One recommendation was that the Board seek the assistance of the American Association of Retired Persons and TRIAD in publicizing and creating awareness of Recovery-related scams, given that perpetrators of scams frequently target the senior population. The Board has since reached out to both of these organizations, as well as the Federal Trade Commission and the National Association of Attorneys General, to establish working relationships and to ensure a general awareness of such schemes. Although we have seen a marked decline in Recovery scams since the initial period of the law's enactment, the Board's relationships with these groups are now in place in the event that new scams arise.

Another suggestion made at the April hearing was that the Board consider employing former journalists to assist with our reporting requirements and to make the Board's website more reader-friendly. Since that hearing, the Board has hired former journalists in various staff positions where their superior writing skills will be put to good use in the Board's required quarterly and annual reports, as well as on the website Recovery.gov.

I am pleased to report that Recovery.gov has been upgraded and its companion reporting website, FederalReporting.gov, has been constructed. FederalReporting.gov, where recipients will enter data on their use of covered funds, has been created, performance-tested, and opened for registration. More than 14,000 recipients have registered with the site since it launched on August 17th. We are encouraging recipients to register prior to October 1, which is when the system will open for reporting purposes. Once data is reported on FederalReporting.gov, it will then flow into the latest iteration of the public-facing website, which I have been referring to as Recovery.gov Version 2.0.

The Board realized at the outset that the redesign and upgrade of Recovery.gov was going to be a project of significant magnitude and complexity. The General Services Administration (GSA) – acting for the Board – used its Alliant Government-Wide Acquisition Contract (GWAC) to select a vendor to redesign Recovery.gov and to rebuild and upgrade the site's infrastructure. The Alliant contract vehicle is designed specifically to support complex IT initiatives, particularly those that need to incorporate new technologies. Previously, 59 companies had won the right to bid on Alliant task orders through open competition. After using

the Alliant vehicle to solicit bids for the redesign, and following an exhaustive evaluation of the bids received, GSA awarded the contract to Smartronix, Inc. of Hollywood, Maryland.

The fully enhanced version of Recovery.gov, which is scheduled for release by October 10<sup>th</sup>, will provide visitors with a visually pleasing, user-friendly, and highly interactive website. It will have a mapping capacity that will allow visitors to search for spending all the way down to their own neighborhoods – or their Congressional districts, for that matter. Even before the newest version of Recovery.gov is unveiled to the public, the Board has implemented various improvements to the site. In July, we began publishing on the website a new regular feature called the Chairman's Corner. There, I inform the American public of the achievements and future plans of the Board, as well as changes and developments made to Recovery.gov. One such change, also added in July, was the addition of an interim mapping solution, which allows the American people to look at major contracts awarded in their areas. This improved mapping system is serving as a placeholder until the final, more versatile mapping solution is introduced next month. Recovery.gov is currently undergoing user testing by citizen focus groups and stakeholders around the country.

As you can sense, I am quite hopeful about the coming capabilities of Recovery.gov Version 2.0, and the data the website will illuminate once Recovery reporting begins in earnest next month. However, I do not believe that just throwing data up on a website qualifies as "transparency." Nor am I under any illusion that the first quarter – or even first few quarters – of reporting will be free of data quality problems.

A distinction needs to be made between data quality and data integrity. Although the Board and Inspectors General (IGs) will play a role in data quality – chiefly by reviewing agencies' processes for ensuring quality of the data – the Board's main goal will be one of data integrity. That is, the Board will strive to ensure that the data on Recovery.gov is a true reflection of what recipients report, including any subsequent modifications made to that data. The Board intends to track changes to the data entered and make that information available on Recovery.gov for all to see. The responsibility for data quality, however, rests with the recipients of the funds and the agencies distributing the funds, as they are in the best position to know the details associated with these funds. IGs' involvement in ensuring data quality could run afoul of the Inspector General Act's longstanding prohibition on program operating responsibilities – as well as the Comptroller General's Government Auditing Standards for performing audits, also known as the Yellow Book.

This manner of data reporting represents new territory and brings the potential for new complications. The government has never before required recipients of federal funds to report to this degree. Even with the informative OMB-sponsored town halls on reporting, the guidance set forth in the OMB memoranda and interim Federal Acquisition Regulation (FAR) rules, and the reporting registry helpdesks that will be ready to receive the influx of questions, there is still potential for reporting issues. These obstacles will need to be overcome. If recipients do not report the required information – for whatever reason, mistake, neglect, or willfulness – the data on Recovery.gov will not be as insightful as it should be, which is a concern that I and the rest of the Board have. Although existing federal laws, like the false statements statute and the recently

amended Civil False Claims Act, should serve as useful tools in deterring willful or reckless noncompliance with the reporting requirements, the most likely outcome may be administrative remedies such as termination of the contract or other negative effects like an adverse past-performance evaluation.

Although the status of Recovery.gov receives a great deal of attention as people attempt to follow expenditures made under the Act, that transparency is only part of the Board's mandate. The Board continues to focus on its mission of accountability and the attendant goal of minimizing fraud, waste, and mismanagement of funds. Before I go on, I would like to expand briefly on my view of "waste" in the context of the Board's mandate. When I state that the Board is trying to minimize waste, I am referring to an objective assessment of contracting practices, rather than a subjective viewpoint of the nature of a particular expenditure. My view is that – aside from being mindful of the Recovery Act's flat-out prohibition on funding for aquariums, zoos, and the like – the purpose of the Board is not to weigh in on spending choices that come down to an agency's judgment or opinion. Such decisions are the result of political and policy determinations made by multiple layers of watchful individuals. Instead, when the Board focuses on waste in the spending of Recovery funds, we will be looking at the incurring of unnecessary costs due to ineffective practices or controls.

To achieve our goal of minimizing fraud, waste, and mismanagement of funds, the Board is coordinating its oversight activities with federal agencies, including IGs, and state officials. For example, the Board is working with OMB to develop a process whereby agencies, OMB, and IGs will work together to identify programs with the highest risk.

One overarching and widely recognized risk is the lack of procurement professionals in the federal government. The Board is keenly aware of this risk, as one of our functions is to review whether agencies have sufficient qualified acquisition and grant personnel overseeing Recovery funds. Without adequate procurement professionals in place to oversee the spending of funds, the likelihood of fraud, waste, and mismanagement only increases. To that end, the Board is partnering with the Office of Personnel Management (OPM) to host a hiring fair targeting procurement, grant, and auditing personnel. This hiring fair will take place here in Washington on October 27th.

As I have said before, the Board's accountability goal is more expansive than merely detecting fraud or waste that has occurred. Rather, given the vast sums that are being distributed, the Board is striving to prevent fraud before it occurs. Given the preponderance of money that will be disbursed by the states, the Board continues to reach out to each state's own Recovery officials, as well as state auditors. Earlier this summer, Board staff attended the National State Auditors Association's annual conference and, in addition to answering generalized questions about navigating the federal process, distributed a Board-prepared Recovery contract compliance checklist, which was well-received as a helpful tool. In addition, I spoke at the Association of Government Accountants' annual meeting in New Orleans alongside a state and city auditor, and last month I spoke at the annual meeting of the National Association of State Auditors, Comptrollers and Treasurers in Michigan. At that latter meeting, a number of technical questions arose, so in response, last week the Board's IT experts hosted a follow-up teleconference for the chief information officers for at least 30 states. These speaking opportunities have allowed me,

other Board members, and Board staff to carry our message beyond the Beltway to where the vast majority of oversight is actually taking place. Finally, the Board is creating a Recovery.gov training website that will contain a list of training opportunities offered by various IGs and other entities. Based on the training available, we will assess the need for the Board to fill any gaps or facilitate training for requesting entities. As Recovery funds continue to flow down the line, the Board will continue to brainstorm new methods to coordinate with and assist state and local governments.

The Board's Accountability Committee continues to strategize regarding methods of not only receiving reports of fraud, waste, and mismanagement and referring them to the appropriate IG, but also analyzing trends in light of publicly available, open-source data. To that end, the Board has recently put out a solicitation for analytical tools and personnel that can best extract and harness existing information in order to make the Board's referrals more value-added for the IGs and also contribute greatly to risk-based predictions about potential fraud. As with our last major procurement, GSA provided our procurement services and for this contract recommended we use the Service-Disabled Veteran-Owned Small Business GWAC. We hope to have our team in place by early October. The tools procured, along with the personnel, will be supervised by federal fraud investigators and will be housed in our Recovery Operations Center. We have high hopes that this risk-based fraud prevention and detection program will serve as a future model for government oversight.

The Board's contracts compliance staff also continues to review Recovery fund procurements as they occur, coordinating with IG offices on myriad issues. Thus far, we have forwarded more than 100 matters to various IGs to ensure heightened scrutiny of specific procurements that Board staff has identified as potentially problematic. These issues range from incidents of administrative oversight to awards that may raise more serious questions requiring resolution.

The Board will also be implementing a hotline where the public can report potential cases of fraud, waste, or mismanagement of Recovery Act funds. After researching several public and private hotline options, the Board has selected a hotline that will allow citizens to call, e-mail, fax, or mail letters to trained operators, and Board staff will then use this information to refer the complaints to the relevant IGs for investigation or other suitable response. We are hopeful that this enhanced hotline solution will be launched in conjunction with the upgraded Recovery.gov.

Whenever citizens have the potential to assist oversight and enforcement entities, legitimate concerns are raised about whistleblower protection. The Recovery Act explicitly states that employees of non-federal employers cannot be fired, demoted, or otherwise discriminated against as punishment for disclosing to the Board or several other entities any information that they believe is evidence of fraud, waste, or gross mismanagement of Recovery Act funds. If citizens believe they are being retaliated against for such disclosures, they may either contact the Board or submit a complaint directly to the appropriate IG.

Mr. Chairman, while I was serving as the IG at the Department of the Interior, I believe I had a well-deserved reputation for aggressively investigating whistleblower complaints of federal employees. I intend now to extend that practice outside the federal arena. If citizens

trust in their government, they will eagerly participate in the transparency and accountability of the Recovery funds. Because I believe that public contributions to transparency and accountability are critical to the Board's success, I plan to do everything I can to earn and keep safe that public trust.

In conclusion, I look forward to returning to this Committee once we have begun to unveil to the American public the full scope of Recovery spending. Those will be interesting times. I do not claim to be a prognosticator, but I suspect that there will be a strong reaction when the American public sees how the government actually spends its money. Some of the instantaneous reaction may be negative, but I think there will be a substantial positive reaction as well. Whatever the short-term effects, however, I truly believe that the long-term effects of such transparency will be decidedly positive. That is why I remain optimistic that the Board and I will be able to achieve success in this grand experiment created by the Recovery Act, and I firmly believe that what we accomplish here will lay the groundwork for how future government spending is tracked.

Mr. Chairman and members of the Committee, that concludes my prepared testimony. Thank you for this opportunity. I will now be glad to answer any questions you might have.

United States Government Accountability Office

GAO

Testimony  
Before the Committee on Homeland  
Security and Governmental Affairs,  
U.S. Senate

For Release on Delivery  
Expected at 10:00 a.m. EDT  
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## RECOVERY ACT

### States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses

Statement of J. Christopher Mihm, Managing Director  
Strategic Issues



GAO-09-908T

## GAO Highlights

Highlights of GAO-09-908T a testimony before the Committee on Homeland Security and Governmental Affairs, U.S. Senate

### Why GAO Did This Study

This testimony is based largely on GAO's July 8, 2009 report, in response to a mandate under the American Recovery and Reinvestment Act of 2009 (Recovery Act). This testimony provides selected updates, including the status of federal Recovery Act outlays. The report addresses: (1) selected states' and localities' uses of Recovery Act funds, (2) the approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of Recovery Act funds. GAO's work for the report is focused on 16 states and certain localities in those jurisdictions as well as the District of Columbia—representing about 66 percent of the U.S. population and two-thirds of the intergovernmental federal assistance available. GAO collected documents and interviewed state and local officials. GAO analyzed federal agency guidance and spoke with Office of Management and Budget (OMB) officials and with program officials at the Centers for Medicare and Medicaid Services, and the Departments of Education, Energy, Housing and Urban Development, Justice, Labor, and Transportation.

### What GAO Recommends

GAO makes recommendations and a matter for congressional consideration discussed on the next page. The report draft was discussed with federal and state officials who generally agreed with its contents. OMB officials generally agreed with GAO's recommendations to OMB. DOT agreed to and has since addressed GAO's recommendation.

View GAO-09-908T, GAO-09-829 or key components. For state summaries, see GAO-09-830SP. For more information, contact J. Christopher Mihm at (202) 512-6806 or mihmj@gao.gov.

September 2009

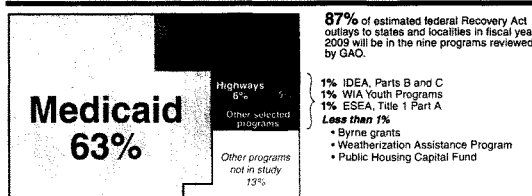
## RECOVERY ACT

### States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses

#### What GAO Found

Across the United States, as of August 28, 2009, Treasury had outlayed about \$45 billion of the estimated \$49 billion in Recovery Act funds projected for use in states and localities in fiscal year 2009. More than three quarters of the federal outlays have been provided through the increased Medicaid Federal Medical Assistance Percentage (FMAP) and the State Fiscal Stabilization Fund (SFSF) administered by the Department of Education.

GAO's work focused on nine federal programs that are estimated to account for approximately 87 percent of federal Recovery Act outlays in fiscal year 2009 for programs administered by states and localities. The following figure shows the distribution by program of anticipated federal Recovery Act spending in fiscal year 2009 for the nine programs discussed in the July report.



Source: GAO analysis of data from CBO and Federal Funds Information for States.

#### Increased Medicaid FMAP Funding

All 16 states and the District have drawn down increased Medicaid FMAP grant awards of just over \$19.6 billion for October 1, 2008, through September 4, 2009, which amounted to almost 84 percent of such funds available to them. All states and the District experienced enrollment growth in this period. Several states noted that the increased FMAP funds were critical in their efforts to maintain coverage at current levels. States and the District reported they are planning to use the increased federal funds to cover their increased Medicaid caseload and to maintain current benefits and eligibility levels. Due to the increased federal share of Medicaid funding, most state officials also said they would use freed-up state funds to help cope with fiscal stresses.

#### Highway Infrastructure Investment

As of September 1, the Department of Transportation (DOT) had obligated approximately \$11 billion for almost 3,800 highway infrastructure and other eligible projects in the 16 states and the District and had reimbursed these 17 jurisdictions about \$604 million. Across the nation, almost half of the obligations have been for pavement improvement projects because they did not require extensive environmental clearances, were quick to design, obligate and bid on, could employ people quickly, and could be completed within 3 years. Officials from most states considered project readiness, including the 3-year completion requirement, when making project selections and only later identified to what extent these projects fulfilled the economically distressed area requirement. We found substantial variation in how states identified economically distressed areas and how they prioritized project selection for

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## Highlights of GAO-09-908T (continued)

these areas. Therefore, GAO recommended that the Secretary of Transportation develop clear guidance on identifying and giving priority to economically distressed areas and more consistent procedures for the Federal Highway Administration (FHWA) to use in reviewing and approving states' criteria. FHWA issued clarifying guidance to address our recommendation in August 2009.

**State Fiscal Stabilization Fund**

As of September 1, 2009, the District and 15 of the 16 states covered by our review had received approval from Education for their initial SFSF funding applications. Pennsylvania had submitted an application to Education, but it had not yet been approved. As of August 28, 2009, Education has made \$21 billion in SFSF grants for Education available to the 15 states and the District—of which over \$7.7 billion had been drawn down as of August 28, 2009. School districts said they would use SFSF funds to maintain current levels of education funding, particularly for retaining staff and current education programs. They also told us that SFSF funds would help offset state budget cuts. Overall, states reported using Recovery Act funds to stabilize state budgets and to cope with fiscal stresses. The funds helped them maintain staffing for existing programs and minimize or avoid tax increases as well as reductions in services.

**Accountability**

States have implemented various internal control programs; however, federal Single Audit guidance and reporting does not fully address Recovery Act risk. The Single Audit reporting deadline is too late to provide audit results in time for the audited entity to take action on deficiencies noted in Recovery Act programs. Moreover, current guidance does not achieve the level of accountability needed to effectively respond to Recovery Act risks. Finally, state auditors need additional flexibility and funding to undertake the added Single Audit responsibilities under the Recovery Act. OMB is vetting a pilot program for early written communication of internal control deficiencies for Recovery Act programs that, if properly scoped to achieve sufficient coverage of Recovery Act programs, could address our concerns about the timeliness of single audit reporting.

**Impact**

Direct recipients of Recovery Act funds, including states and localities, are expected to report quarterly on a number of measures, including the use of funds and estimates of the number of jobs created and retained. The first of these reports is due in October 2009. OMB—in consultation with a range of stakeholders—issued additional implementing guidance for recipient reporting on June 22, 2009, that clarifies some requirements and establishes a central reporting framework.

In addition to employment-related reporting, OMB requires reporting on the use of funds by recipients and nonfederal subrecipients receiving Recovery Act funds.

The tracking of funds is consistent with the Federal Funding Accountability and Transparency Act (FFATA). Like the Recovery Act, FFATA requires a publicly available Web site—[www.USAspending.gov](http://www.USAspending.gov)—to report financial information about entities awarded federal funds. Yet, significant questions have been raised about the reliability of the data on [www.USAspending.gov](http://www.USAspending.gov), primarily because what is reported by the prime recipients is dependent on the unknown data quality and reporting capabilities of subrecipients.

**GAO's Recommendations**

**Accountability and Transparency:** To leverage Single Audits as an effective oversight tool for Recovery Act programs, the Director of OMB should

- develop requirements for reporting on internal controls during 2009 before significant Recovery Act expenditures occur, as well as for ongoing reporting after the initial report;
- provide more direct focus on Recovery Act programs through the Single Audit to help ensure that smaller programs with high risk have audit coverage in the area of internal controls and compliance;
- evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act;
- develop mechanisms to help fund the additional Single Audit costs and efforts for auditing Recovery Act programs; and
- take steps to achieve sufficient participation and coverage in the single audit pilot program that provides for early written communication of internal control deficiencies to achieve the objective of more timely accountability over Recovery Act funds.

**Matter for Congressional Consideration:** Congress should consider a mechanism to help fund the additional Single Audit costs and efforts for auditing Recovery Act programs.

**Reporting on Impact:** The Director of OMB should work with federal agencies to provide recipients with examples of the application of OMB's guidance on recipient reporting of jobs created and retained. In addition, the Director of OMB should work with agencies to clarify what new or existing program performance measures are needed to assess the impact of Recovery Act funding.

**Communications and Guidance:** To strengthen the effort to track funds and their uses, the Director of OMB should continue efforts to ensure more direct communication with key state officials, and in addition, (1) provide a long range time line on issuing federal guidance, (2) clarify what constitutes appropriate quality control and reconciliation by prime recipients, and (3) specify who should best provide formal certification and approval of the data reported.

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Mr. Chairman, Ranking Member Collins, and Members of the Committee:

I am pleased to be here today to discuss our work examining the uses and planning by selected states and localities for funds made available by the American Recovery and Reinvestment Act of 2009 (Recovery Act).<sup>1</sup> As federal funds provided by the Recovery Act flow into the U.S. economy, state fiscal conditions continue to be stressed. Actual declines in sales, personal income, and corporate income tax revenues influenced state actions to begin to fill an estimated \$230 billion in budget gaps for fiscal years 2009 through 2011.<sup>2</sup> The national unemployment rate also increased to 9.5 percent in June 2009, and high unemployment can place greater stress on state budgets as demand for services, such as Medicaid, increases. Some economists have pointed to signs of economic improvement, although associations representing state officials have also reported that state fiscal conditions historically lag behind any national economic recovery.

The Recovery Act specifies several roles for GAO, including conducting bimonthly reviews of selected states' and localities' use of funds made available under the act.<sup>3</sup> The report that we issued on July 8th, the second in response to the act's mandate, addressed the following objectives: (1) selected states' and localities' uses of Recovery Act funds, (2) the approaches taken by the selected states and localities to ensure accountability for Recovery Act funds, and (3) states' plans to evaluate the impact of the Recovery Act funds they received.<sup>4</sup> The report provides overall findings, makes recommendations, and discusses the status of actions in response to the recommendations we made in our April 2009 report.<sup>5</sup> Individual summaries for the 16 selected states and the District of Columbia (District) are accessible through GAO's recovery page at

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<sup>1</sup>Pub. L. No. 111-5, 123 Stat. 115 (February 17, 2009).

<sup>2</sup>The estimated budget gaps are reported by associations representing state officials. See The National Governors Association and the National Association of State Budget Officers, *The Fiscal Survey of States* (Washington, D.C., June 2009).

<sup>3</sup>Recovery Act, div. A, title IX, §901.

<sup>4</sup>GAO, *Recovery Act: States' and Localities' Current and Planned Uses of Funds While Facing Fiscal Stresses*, GAO-09-829 (Washington, D.C.: Jul. 8, 2009).

<sup>5</sup>GAO, *Recovery Act: As Initial Implementation Unfolds in States and Localities, Continued Attention to Accountability Issues Is Essential*, GAO-09-580 (Washington, D.C.: Apr. 23, 2009).

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[www.gao.gov/recovery](http://www.gao.gov/recovery). In addition, all of the summaries have been compiled into an electronic supplement, GAO-09-830SP.

As reported in our April 2009 review, to address these objectives, we selected a core group of 16 states and the District that we will follow over the next few years.<sup>6</sup> Our bimonthly reviews examine how Recovery Act funds are being used and whether they are achieving the stated purposes of the act. These purposes include

- to preserve and create jobs and promote economic recovery;
- to assist those most impacted by the recession;
- to provide investments needed to increase economic efficiency by spurring technological advances in science and health;
- to invest in transportation, environmental protection, and other infrastructure that will provide long-term economic benefits; and
- to stabilize state and local government budgets, in order to minimize and avoid reductions in essential services and counterproductive state and local tax increases.

The states selected for our bimonthly reviews contain about 65 percent of the U.S. population and are estimated to receive collectively about two-thirds of the intergovernmental federal assistance funds available through the Recovery Act. We selected these states and the District on the basis of federal outlay projections, percentage of the U.S. population represented, unemployment rates and changes, and a mix of states' poverty levels, geographic coverage, and representation of both urban and rural areas. In addition, we visited a nonprobability sample of more than 175 local entities within the 16 selected states and the District.<sup>7</sup>

GAO's work for this report focused on nine federal programs primarily because they have begun disbursing funds to states or have known or

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<sup>6</sup>The states we are following as part of our analysis are Arizona, California, Colorado, Florida, Georgia, Illinois, Iowa, Massachusetts, Michigan, Mississippi, New Jersey, New York, North Carolina, Ohio, Pennsylvania, and Texas.

<sup>7</sup>This total includes two entities in the District of Columbia that received direct federal funding that was not passed through the District government.

potential risks.<sup>8</sup> These risks can include existing programs receiving significant amounts of Recovery Act funds or new programs. We collected documents from and conducted semistructured interviews with executive-level state and local officials and staff from state offices including governors' offices, "recovery czars," state auditors, and controllers. In addition, our work focused on federal, state, and local agencies administering the selected programs receiving Recovery Act funds. We analyzed guidance and interviewed officials from the federal Office of Management and Budget (OMB). We also analyzed other federal agency guidance on programs selected for this review and spoke with relevant program officials at the Centers for Medicare and Medicaid Services (CMS), the U.S. Departments of Education, Energy, Housing and Urban Development, Justice, Labor, and Transportation. Where attributed to state officials, we did not review state legal materials for this report, but relied on state officials and other state sources for description and interpretation of relevant state constitutions, statutes, legislative proposals, and other state legal materials. The information obtained from this review cannot be generalized to all states and localities receiving Recovery Act funding. A detailed description of our scope and methodology can be found in appendix 1 of the full report.

We conducted this performance audit from April 21, 2009 to July 2, 2009, and selectively updated data, where available, for this statement in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## Background

Our analysis of initial estimates of Recovery Act spending provided by the Congressional Budget Office (CBO) suggested that about \$49 billion would be outlayed to states and localities by the federal government in fiscal year

<sup>8</sup>For this report, GAO reviewed states' and localities' uses of Recovery Act funds for the (1) Medicaid Federal Medical Assistance Percentage (FMAP), (2) the State Fiscal Stabilization Fund (SFSF), (3) the Federal-Aid Highway Surface Transportation Program, (4) Public Housing Capital Fund, (5) Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA), (6) Parts B and C of the Individuals with Disabilities Education Act (IDEA), (7) Weatherization Assistance Program, (8) Edward Byrne Memorial Justice Assistance Grant (JAG) Program, and (9) Workforce Investment Act (WIA) Youth Program.

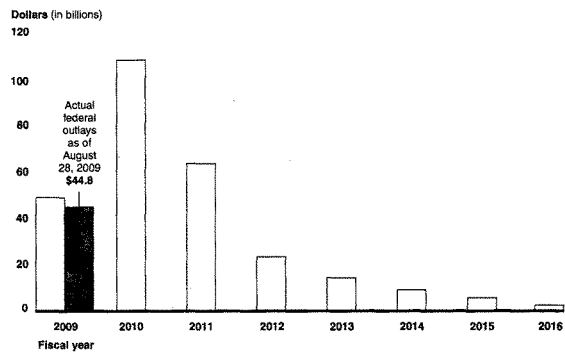
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2009, which runs through September 30. However, our analysis of actual federal outlays reported on [www.recovery.gov](http://www.recovery.gov)<sup>a</sup> at the time of our bimonthly review indicated that in the 4 months since enactment, the federal Treasury had paid out approximately \$29 billion to states and localities, which was about 60 percent of the payments estimated for fiscal year 2009. Since the release of our July report, an additional \$16 billion in Recovery Act funds has been outlayed to states and localities during that period for a total of almost \$45 billion as of August 28, 2009. Although this pace of spending may not continue for the remainder of the fiscal year, at present spending is slightly ahead of the original estimates. Figure 1 shows the original estimate of federal outlays to states and localities under the Recovery Act compared with actual federal outlays as reported by federal agencies on [www.recovery.gov](http://www.recovery.gov). More than three quarters of the \$45 billion in federal outlays has been provided through the increased Federal Medical Assistance Percentage (FMAP) grant awards and the State Fiscal Stabilization Fund administered by the Department of Education. Figure 1 shows actual federal outlays as of August 28, 2009 and the original estimate. According to the Office of Management and Budget (OMB), an estimated \$149 billion in Recovery Act funding will be obligated to states and localities in fiscal year 2009.

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<sup>a</sup>The Web site [www.recovery.gov](http://www.recovery.gov) is mandated by the Recovery Act to foster greater accountability and transparency in the use of the act's funds. The Web site is required to include plans from federal agencies; information on federal awards of formula grants and awards of competitive grants; and information on federal allocations for mandatory and other entitlement programs by state, county, or other appropriate geographical unit. The Web site is maintained by the Recovery Accountability and Transparency Board.

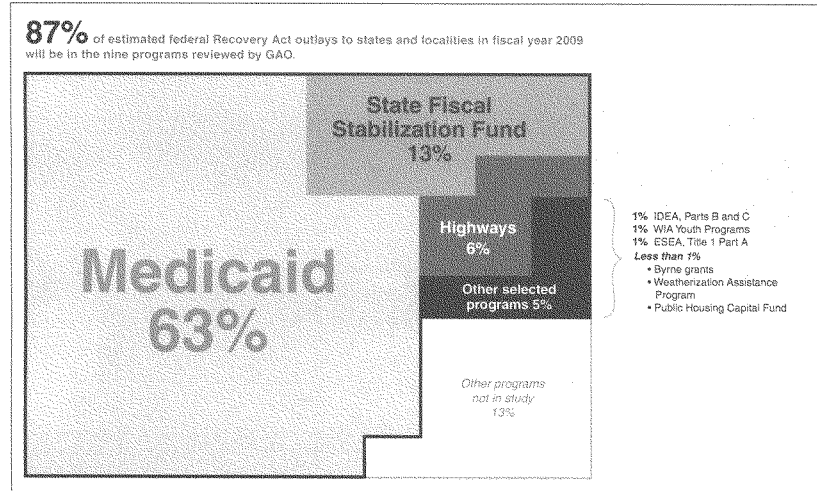
**Figure 1: Projected versus Actual Federal Outlays to States and Localities under the Recovery Act**



Source: GAO analysis of CBO, Federal Funds Information for States, and Recovery.gov data.

Our work for our July bimonthly report focused on nine federal programs, selected primarily because they have begun disbursing funds to states and include programs with significant amounts of Recovery Act funds, programs receiving significant increases in funding, and new programs. Recovery Act funding of some of these programs is intended for further disbursement to localities. Together, these nine programs are estimated to account for approximately 87 percent of federal Recovery Act outlays to state and localities in fiscal year 2009. Figure 2 shows the distribution by program of anticipated federal Recovery Act spending in fiscal year 2009 to states and localities.

**Figure 2: Programs in July Review, Estimated Federal Recovery Act Outlays to States and Localities in Fiscal Year 2009 as a Share of Total**



Source: GAO analysis of data from CBO and Federal Funds Information for States.

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**States and Localities  
Are Using Recovery  
Act Funds for  
Purposes of the Act  
and to Help Address  
Fiscal Stresses**

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**Increased FMAP Has  
Helped States Finance  
Their Growing Medicaid  
Programs, but Concerns  
Remain about Compliance  
with Recovery Act  
Provisions**

The Recovery Act provides eligible states with an increased FMAP for 27 months between October 1, 2008, and December 31, 2010.<sup>10</sup> On February 25, 2009, CMS made increased FMAP grant awards to states, and states may retroactively claim reimbursement for expenditures that occurred prior to the effective date of the Recovery Act.

For the third quarter of fiscal year 2009, the increases in FMAP for the 16 states and the District of Columbia compared with the original fiscal year 2009 levels are estimated to range from 6.2 percentage points in Iowa to 12.24 percentage points in Florida, with the FMAP increase averaging just over 10 percentage points. When compared with the first two quarters of

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<sup>10</sup>Recovery Act, div. B, title V, § 5001. Medicaid is a joint federal-state program that finances health care for certain categories of low-income individuals, including children, families, persons with disabilities, and persons who are elderly. The federal government matches state spending for Medicaid services according to a formula based on each state's per capita income in relation to the national average per capita income. The rate at which states are reimbursed for Medicaid service expenditures is known as the FMAP, which may range from 50 percent to no more than 83 percent. Generally, for fiscal year 2009 through the first quarter of fiscal year 2011, the increased FMAP, which is calculated on a quarterly basis, provides for (1) the maintenance of states' prior year FMAPs, (2) a general across-the-board increase of 6.2 percentage points in states' FMAPs, and (3) a further increase to the FMAPs for those states that have a qualifying increase in unemployment rates. The increased FMAP available under the Recovery Act is for state expenditures for Medicaid services. However, the receipt of this increased FMAP may reduce the funds that states would otherwise have to use for their Medicaid programs, and states have reported using these available funds for a variety of purposes.



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fiscal year 2009, the FMAP in the third quarter of fiscal year 2009 increased in 12 of the 16 states and the District.<sup>11</sup>

From October 2007 to May 2009, overall Medicaid enrollment in the 16 states and the District increased by 7 percent.<sup>12</sup> In addition, each of the states and the District experienced an enrollment increase during this period, with the highest number of programs experiencing an increase of 5 percent to 10 percent. However, the percentage increase in enrollment varied widely ranging from just under 3 percent in California to nearly 20 percent in Colorado.

Since our July report and with regard to the states' receipt of the increased FMAP, all 16 states and the District had drawn down increased FMAP grant awards of just over \$19.6 billion for the period of October 1, 2008 through September 4, 2009, which amounted to almost 84 percent of funds available. In addition, except for the initial weeks that increased FMAP funds were available, the weekly rate at which the sample states and the District have drawn down these funds has remained relatively constant.

States reported that they are using or are planning to use the funds that have become freed up as a result of increased FMAP for a variety of purposes. Most commonly, states reported that they are using or planning to use freed-up funds to cover their increased Medicaid caseload, to maintain current benefits and eligibility levels, and to help finance their respective state budgets. Several states noted that given the poor economic climate in their respective states, these funds were critical in their efforts to maintain Medicaid coverage at current levels.

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<sup>11</sup>In an August 4, 2009, Federal Register Notice, HHS published a change to the methodology it uses to calculate the increased FMAP rates. Under this methodology, HHS calculates preliminary FMAP rates prior to the start of each quarter using Bureau of Labor Statistics preliminary unemployment estimates, and CMS uses these FMAP rates to determine adjustments to the quarterly increased FMAP grant awards. Once final unemployment numbers become available, HHS publishes the final FMAP rates and CMS awards are adjusted, as necessary. Under the new methodology, the FMAP rate for the third quarter of fiscal year 2009 increased in 4 of our 17 sample states.

<sup>12</sup>The percentage increase is based on actual state enrollment data for October 2007 to April 2009 and projected enrollment data for May 2009, with the exception of New York, which provided projected enrollment data for March, April and May 2009. Three states—Florida, Georgia, and Mississippi—did not provide projected enrollment data for May 2009. We estimated enrollment for these states for May 2009 to determine the total change in enrollment for October 2007 to May 2009.

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While officials from several states spoke positively about CMS's guidance related to FMAP requirements, over half of the states and the District reported they wanted CMS to provide additional guidance regarding how they report monthly on increased FMAP spending and whether certain programmatic changes would affect their eligibility for funds. For example, Medicaid officials from several states told us they were hesitant to implement minor programmatic changes, such as changes to prior authorization requirements, pregnancy verifications, or ongoing rate changes, out of concern that doing so would jeopardize their eligibility for increased FMAP. In addition, at least three states raised concerns that glitches related to new or updated information systems used to generate provider payments could affect their eligibility for these funds.

Due to the variability of state operations, funding processes, and political structures, CMS has worked with states on a case-by-case basis to discuss and resolve issues that arise. Specifically, communications between CMS and several states indicate efforts to clarify issues related to the contributions to the state share of Medicaid spending by political subdivisions or to rainy-day funds. Since we issued our July report, on July 30, 2009, CMS published new guidance for states regarding the prompt payment requirement. The guidance describes the method states should use to calculate days during a quarter that states have either met or not met the prompt payment requirement in the Medicaid statute; and how a state could obtain a waiver from the requirement. More recently, CMS published new guidance clarifying the maintenance of eligibility requirements under the Recovery Act, which includes a discussion of programmatic changes that could affect states' eligibility for the increased FMAP.<sup>15</sup>

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<sup>15</sup> As of September 4, 2009, these publications were available on the CMS website; see <http://www.cms.hhs.gov/SMDL/SMD/list.asp?sortByDID=1a&submit=Go&filterType=none&filterByDID=90&sortOrder=ascending&intNumPerPage=10>.

**States Are Using Highway Infrastructure Funds Mainly for Pavement Improvements and Are Generally Complying with Recovery Act Requirements**

The Recovery Act provides funding to the states for restoration, repair, and construction of highways and other eligible surface transportation projects. The act requires that 30 percent of these funds be suballocated, primarily based on population, for metropolitan, regional, and local use.<sup>14</sup> In March 2009, \$26.7 billion was apportioned to all 50 states and the District of Columbia (District) for highway infrastructure and other eligible projects. More recently, as of September 1, 2009, \$18 billion of the funds had been obligated<sup>15</sup> for almost 7,000 projects nationwide, and approximately \$11 billion had been obligated for almost 3,800 projects in the 16 states and the District that are the focus of GAO's review.

Almost half of Recovery Act highway obligations nationwide have been for pavement improvements. Specifically, \$8.7 billion of the \$ 18 billion obligated nationwide is being used for projects such as reconstructing or rehabilitating deteriorated roads. Many state officials told us they selected a large percentage of resurfacing and other pavement improvement projects because they did not require extensive environmental clearances, were quick to design, could be quickly obligated and bid, could employ people quickly, and could be completed within 3 years. In addition, \$3 billion, or about 16 percent of Recovery Act funds nationally, has been obligated for pavement-widening projects and around 10 percent has been obligated for the replacement, improvement or rehabilitation of bridges.<sup>16</sup>

As of September 1, 2009, \$1.4 billion had been reimbursed nationwide by the Federal Highway Administration (FHWA) and \$604 million had been reimbursed in the 16 states and the District. States are just beginning to get projects awarded so that contractors can begin work, and U.S. Department

<sup>14</sup>Highway funds are apportioned to the states through federal-aid highway program mechanisms, and states must follow the requirements of the existing program, which include ensuring the project meets all environmental requirements associated with the National Environmental Policy Act (NEPA), paying a prevailing wage in accordance with federal Davis-Bacon requirements, complying with goals to ensure disadvantaged businesses are not discriminated against in the awarding of construction contracts, and using American-made iron and steel in accordance with Buy America program requirements. However, the maximum federal fund share of highway infrastructure investment projects under the Recovery Act is 100 percent, while the federal share under the existing federal-aid highway program is generally 80 percent.

<sup>15</sup>The U.S. Department of Transportation has interpreted the term obligation of funds to mean the federal government's contractual commitment to pay for the federal share of the project. This commitment occurs at the time the federal government signs a project agreement.

<sup>16</sup>Data are as of July 10, 2009.

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of Transportation (DOT) officials told us that although funding has been obligated for almost 7,000 projects, it may be months before states can request reimbursement. Once contractors mobilize and begin work, states make payments to these contractors for completed work, and may request reimbursement from FHWA. FHWA told us that once funds are obligated for a project, it may take 2 or more months for a state to bid and award the work to a contractor and have work begin.

According to state officials, because an increasing number of contractors are looking for work, bids for Recovery Act contracts have come in under estimates. State officials told us that bids for the first Recovery Act contracts were ranging from around 5 percent to 30 percent below the estimated cost. Several state officials told us they expect this trend to continue until the economy substantially improves and contractors begin taking on enough other work.

Funds appropriated for highway infrastructure spending must be used as required by the Recovery Act. States are required to do the following:

- Ensure that 50 percent of apportioned Recovery Act funds are obligated within 120 days of apportionment (before June 30, 2009) and that the remaining apportioned funds are obligated within 1 year. The 50 percent rule applies only to funds apportioned to the state and not to the 30 percent of funds required by the Recovery Act to be suballocated, primarily based on population, for metropolitan, regional, and local use. The Secretary of Transportation is to withdraw and redistribute to other states any amount that is not obligated within these time frames.<sup>17</sup>
- Give priority to projects that can be completed within 3 years and to projects located in economically distressed areas. These areas are defined by the Public Works and Economic Development Act of 1965, as amended.<sup>18</sup> According to the act, to qualify as economically distressed, an area must have (1) a per capita income that is 80 percent or less than the national average or (2) an unemployment rate that is, for the most recent 24-month period for which data are available, at

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<sup>17</sup>Recovery Act, Pub. L. No. 111-5, div. A, title XII, 123 Stat. 115, 206 (Feb. 17, 2009).

<sup>18</sup>*Id.*

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least 1 percent greater than the national average.<sup>19</sup> For areas that do not meet one of these two criteria, the Secretary of Commerce has the authority to determine that an area has experienced or is about to experience a "special need" arising from actual or threatened severe unemployment or economic adjustment problems.

- Certify that the state will maintain the level of spending for the types of transportation projects funded by the Recovery Act that it planned to spend the day the Recovery Act was enacted. As part of this certification, the governor of each state is required to identify the amount of funds the state plans to expend from state sources from February 17, 2009, through September 30, 2010.<sup>20</sup>

All states have met the first Recovery Act requirement that 50 percent of their apportioned funds are obligated within 120 days. Of the \$18.7 billion nationally that is subject to this provision, 75 percent was obligated as of September 1, 2009.

The second Recovery Act requirement is to give priority to projects that can be completed within 3 years and to projects located in economically distressed areas. While officials from almost all of the states we reviewed said that they considered project readiness, including the 3-year completion requirement, when making project selections, there was substantial variation in the extent to which states prioritized projects in economically distressed areas and how they identified these areas. Many states based their project selections on other factors and only later identified whether these projects were in economically distressed areas. We reported in July that DOT and FHWA had not provided clear guidance—while officials emphasized the importance of giving priority to these areas, it did not define what giving priority meant, and thus did not ensure that the act's priority provisions would be consistently applied. We also found instances of states developing their own eligibility requirements for economically distressed areas using data or criteria not specified in the Public Works and Economic Development Act. For example, one state

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<sup>19</sup>42 U.S.C. § 3161(a). Eligibility must be supported using the most recent federal data available or, in the absence of recent federal data, by the most recent data available through the government of the state in which the area is located. Federal data that may be used include data reported by the Bureau of Economic Analysis, the Bureau of Labor Statistics, the Census Bureau, the Bureau of Indian Affairs, or any other federal source determined by the Secretary of Commerce to be appropriate (42 U.S.C. § 3161((c)).

<sup>20</sup>Recovery Act, div. A, title XII, § 1201.

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identified these areas based in part on home foreclosure rates—data not specified in the Public Works Act. In each of the cases we identified, the states informed us that FHWA approved the state's use of alternative criteria. However, FHWA did not consult with or seek the approval of the Department of Commerce, and it was not clear under what authority FHWA approved these criteria. As a result we recommended that the Secretary of Transportation, in consultation with the Secretary of Commerce, develop (1) clear guidance on identifying and giving priority to economically distressed areas, and (2) more consistent procedures for FHWA to use in reviewing and approving states' criteria for designating distressed areas.

In response to the recommendation in our July report, FHWA, in consultation with the Department of Commerce, developed guidance that addresses our recommendation. In particular, FHWA's August 2009 guidance directs states to give priority to projects that are located in an economically distressed area and can be completed within the 3-year timeframe over other projects. In the guidance, FHWA also directs states to maintain information as to how they identified, vetted, examined, and selected projects located in economically distressed areas. In addition, FHWA's guidance sets out criteria that states may use to identify economically distressed areas based on "special need." The criteria aligns closely with criteria used by the Department of Commerce's Economic Development Administration (EDA) in designating special needs areas in its own grant programs, including factors such as actual or threatened business closures (including job loss thresholds), military base closures, and natural disasters or emergencies. According to EDA, while the agency traditionally approves special needs designations on a case-by-case basis for its own grant program, it does not have the resources to do so for the purpose of Recovery Act highway funding.<sup>21</sup> Rather, in supplemental guidance issued August 24, 2009, FHWA required states to document their reliance on "special need" criteria and provide the documentation to FHWA Division Offices, thereby making the designation of new "special need" areas for the for Recovery Act highway funding "self executing" by the states, meaning the states will apply the criteria laid out in the guidance to identify these areas. We plan to continue to monitor FHWA's and the states' implementation of the economically distressed area

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<sup>21</sup> FHWA's guidance specifies that special needs determinations will be solely for Recovery Act highway funding and will not apply to EDA grant programs.

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requirement, including the states' application of the special needs criteria, in our future reviews.

Finally, the states are required to certify that they will maintain the level of state effort for programs covered by the Recovery Act. With one exception, the states have completed these certifications, but they face challenges. Maintaining a state's level of effort can be particularly important in the highway program. We have found that the preponderance of evidence suggests that increasing federal highway funds influences states and localities to substitute federal funds for funds they otherwise would have spent on highways.<sup>22</sup> As we previously reported, substitution makes it difficult to target an economic stimulus package so that it results in a dollar-for-dollar increase in infrastructure investment.<sup>23</sup>

Most states revised the initial certifications they submitted to DOT. As we reported in April, many states submitted explanatory certifications—such as stating that the certification was based on the “best information available at the time”—or conditional certifications, meaning that the certification was subject to conditions or assumptions, future legislative action, future revenues, or other conditions. On April 22, 2009, the Secretary of Transportation sent a letter to each of the nation's governors and provided additional guidance, including that conditional and explanatory certifications were not permitted, and gave states the option of amending their certifications by May 22. All states and the District have submitted their certifications. According to DOT officials, the department has concluded that the form of each certification is consistent with the additional guidance. While DOT has concluded that the form of the revised certifications is consistent with the additional guidance, it is evaluating the

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<sup>22</sup>In 2004, we estimated that during the 1983 through 2000 period, states used roughly half of the increases in federal highway funds to substitute for funding they would otherwise have spent from their own resources and that the rate of substitution increased during the 1990s. The federal-aid highway program creates the opportunity for substitution because states typically spend substantially more than the amount required to meet federal matching requirements. As a consequence, when federal funding increases, states are able to reduce their own highway spending and still obtain increased federal funds. The federal share under the existing federal-aid highway program is generally 80 percent and the matching requirement for states is usually 20 percent. In 2004, we reported that in 2002, states and localities contributed 54 percent of the nation's capital investment in highways, while the federal government contributed 46 percent (in 2001 dollars). GAO, *Federal-Aid Highways: Trends, Effect on State Spending, and Options for Future Program Design*, GAO-04-802 (Washington, D.C.: Aug. 31, 2004).

<sup>23</sup>GAO, *Physical Infrastructure: Challenges and Investment Options for the Nation's Infrastructure*, GAO-08-763T (Washington, D.C.: May 8, 2008).

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states' method of calculating the amounts they planned to expend for the covered programs and the reasonableness of these numbers. \*

States face drastic fiscal challenges, and most states are estimating that their fiscal year 2009 and 2010 revenue collections will be well below estimates. In the face of these challenges, some states told us that meeting the maintenance-of-effort requirements over time poses significant challenges. For example, federal and state transportation officials in Illinois told us that to meet its maintenance-of-effort requirements in the face of lower-than-expected fuel tax receipts, the state would have to use general fund or other revenues to cover any shortfall in the level of effort stated in its certification. Mississippi transportation officials are concerned about the possibility of statewide, across-the-board spending cuts in 2010. According to the Mississippi transportation department's budget director, the agency will try to absorb any budget reductions in 2010 by reducing administrative expenses to maintain the state's level of effort.



**Most States We Visited  
Have Received State Fiscal  
Stabilization Funds and  
Have Planned to Allocate  
Most Education  
Stabilization Funds to  
LEAs**

The Recovery Act created a State Fiscal Stabilization Fund (SFSF) in part to help state and local governments stabilize their budgets by minimizing budgetary cuts in education and other essential government services, such as public safety.<sup>24</sup> Beginning in March 2009, the Department of Education issued a series of fact sheets, letters, and other guidance to states on the SFSF. Specifically, a March fact sheet, the Secretary's April letter to Governors, and program guidance issued in April and May mention that the purposes of the SFSF include helping stabilize state and local budgets, avoiding reductions in education and other essential services, and ensuring LEAs and public IHEs have resources to "avert cuts and retain teachers and professors." The documents also link educational progress to economic recovery and growth and identify four principles to guide the distribution and use of Recovery Act funds: (1) spend funds quickly to retain and create jobs; (2) improve student achievement through school improvement and reform; (3) ensure transparency, public reporting, and accountability; and (4) invest one-time Recovery Act funds thoughtfully to avoid unsustainable continuing commitments after the funding expires, known as the "funding cliff."

<sup>24</sup>Stabilization funds for education distributed under the Recovery Act must be used to alleviate shortfalls in state support for education to school districts and public institutions of higher education (IHEs). The U.S. Department of Education (Education), the federal agency charged with administration and oversight of the SFSF, distributes the funds on a formula basis, with 81.8 percent of each state's allocation designated for the education stabilization fund for local educational agencies (LEA) and public IHEs. The remaining 18.2 percent of each state's allocation is designated for the government services fund for public safety and other government services, which may include education. Consistent with the purposes of the Recovery Act—which include, in addition to stabilizing state and local budgets, promoting economic recovery and preserving and creating jobs—the SFSF can be used by states to restore cuts to state education spending. In return for SFSF funding, a state must make several assurances, including that it will maintain state support for education at least at fiscal year 2006 levels. In order to receive SFSF funds, each state must also assure it will implement strategies to advance education reform in four specific ways as described by Education: 1) Increase teacher effectiveness and address inequities in the distribution of highly qualified teachers; 2) Establish a pre-K-through-college data system to track student progress and foster improvement; 3) Make progress toward rigorous college- and career-ready standards and high-quality assessments that are valid and reliable for all students, including students with limited English proficiency and students with disabilities; and 4) Provide targeted, intensive support and effective interventions to turn around schools identified for corrective action or restructuring. Schools identified for corrective action have missed academic targets for 4 consecutive years and schools implementing restructuring have missed academic targets for 6 consecutive years. Along with these education reform assurances, additional state assurances must address federal requirements concerning accountability, transparency, reporting, and compliance with certain federal laws and regulations.

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After meeting assurances to maintain state support for education at least at fiscal year 2006 levels, states are required to use the education stabilization fund to restore state support to the greater of fiscal year 2008 or 2009 levels for elementary and secondary education, public IHEs, and, if applicable, early childhood education programs. States must distribute these funds to school districts using the primary state education formula but maintain discretion in how funds are allocated to public IHEs. If, after restoring state support for education, additional funds remain, the state must allocate those funds to school districts according to the Elementary and Secondary Education Act of 1965 (ESEA), Title I, Part A funding formula. On the other hand, if a state's education stabilization fund allocation is insufficient to restore state support for education, then a state must allocate funds in proportion to the relative shortfall in state support to public school districts and public IHEs. Education stabilization funds must be allocated to school districts and public IHEs and cannot be retained at the state level.

Once education stabilization funds are awarded to school districts and public IHEs, they have considerable flexibility over how they use those funds. School districts are allowed to use education stabilization funds for any allowable purpose under ESEA, the Individuals with Disabilities Education Act (IDEA), the Adult Education and Family Literacy Act, or the Carl D. Perkins Career and Technical Education Act of 2006 (Perkins Act), subject to some prohibitions on using funds for, among other things, sports facilities and vehicles. In particular, Education's guidance states that because allowable uses under the Impact Aid provisions of ESEA are broad, school districts have discretion to use education stabilization funds for a broad range of things, such as salaries of teachers, administrators, and support staff, and purchases of textbooks, computers, and other equipment. The Recovery Act allows public IHEs to use education stabilization funds in such a way as to mitigate the need to raise tuition and fees, as well as for the modernization, renovation, and repair of facilities, subject to certain limitations. However, the Recovery Act prohibits public IHEs from using education stabilization funds for such things as increasing endowments; modernizing, renovating, or repairing sports facilities; or maintaining equipment. Education's SFSF guidance expressly prohibits states from placing restrictions on LEAs' use of education stabilization funds, beyond those in the law, but allows states some discretion in placing limits on how IHEs may use these funds.

The SFSF provides states and school districts with additional flexibility, subject to certain conditions, to help them address fiscal challenges. For example, the Secretary of Education is granted authority to permit waivers

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of state maintenance-of-effort (MOE) requirements if a state certified that state education spending will not decrease as a percentage of total state revenues. Education issued guidance on the MOE requirement, including the waiver provision, on May 1, 2009. Also, the Secretary may permit a state or school district to treat education stabilization funds as nonfederal funds for the purpose of meeting MOE requirements for any program administered by Education, subject to certain conditions.

States have broad discretion over how the \$8.8 billion in the SFSF government services fund are used. The Recovery Act provides that these funds must be used for public safety and other government services and that these services may include assistance for education, as well as modernization, renovation, and repairs of public schools or IHEs.

On April 1, 2009, Education made at least 67 percent of each state's SFSF funds<sup>25</sup> available, subject to the receipt of an application containing state assurances, information on state levels of support for education and estimates of restoration amounts, and baseline data demonstrating state status on each of the four education reform assurances. If a state could not certify that it would meet the MOE requirement, Education required it to certify that it will meet requirements for receiving a waiver—that is, that education spending would not decrease relative to total state revenues. In determining state level of support for elementary and secondary education, Education required states to use their primary formula for distributing funds to school districts but also allowed states some flexibility in broadening this definition. For IHEs, states have some discretion in how they establish the state level of support, with the provision that they cannot include support for capital projects, research and development, or amounts paid in tuition and fees by students. In order to meet statutory requirements for states to establish their current status regarding each of the four required programmatic assurances, Education provided each state with the option of using baseline data Education had identified or providing another source of baseline data. Some of the data provided by Education was derived from self-reported data submitted annually by the states to Education as part of their Consolidated State Performance Reports (CSPR), but Education also relied on data from third

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<sup>25</sup>This was phase I funding. A state will receive the remaining allotment of its SFSF allocation in phase II after Education approves the state's comprehensive plan for making progress with respect to the four education reform assurances.

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parties, including the Data Quality Campaign (DQC), the National Center for Educational Achievement (NCEA), and Achieve.<sup>26</sup>

Education has reviewed applications as they arrive for completeness and has awarded states their funds once it determined all assurances and required information had been submitted. Education set the application deadline for July 1, 2009. On June 24, 2009, Education issued guidance to states informing them they must amend their applications if there are changes to the reported levels of state support that were used to determine maintenance of effort or to calculate restoration amounts.

As an update to our July report, as of September 1, 2009, the District and 15 of the states covered by our review had received approval from Education for their initial SFSF funding applications. Pennsylvania had submitted an application to Education but it had not yet been approved. As of August 28, 2009, Education had made \$21 billion in SFSF grants for Education available to the 15 states and the District. As of August 28, 2009, 14 of these states had drawn down SFSF Recovery Act funds. In total, over \$7.7 billion, or about 36 percent of available funds had been drawn down by these states as of August 28, 2009.

Three of the selected states—Florida, Massachusetts, and New Jersey—said they would not meet the maintenance-of-effort requirements but would meet the eligibility requirements for a waiver and that they would apply for a waiver. Most of the states' applications show that they plan to provide the majority of education stabilization funds to LEAs, with the remainder of funds going to IHEs. Several states and the District of Columbia estimated in their application that they would have funds remaining beyond those that would be used to restore education spending in fiscal years 2009 and 2010. These funds can be used to restore education spending in fiscal year 2011, with any amount left over to be distributed to LEAs.

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<sup>26</sup>DQC is a national collaborative effort involving more than 50 organizations working to encourage and support state policymakers to improve the availability and use of high-quality education data to improve student achievement. NCEA, a nonprofit organization owned by ACT Inc.—a company that develops and markets assessments—focuses on raising student achievement based on higher college and career readiness standards. Achieve, created in 1996 by the nation's governors and corporate leaders, is an independent, bipartisan, nonprofit education reform organization focused on raising academic standards and graduation requirements, improving assessments, and strengthening accountability.

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States have flexibility in how they allocate education stabilization funds among IHEs but, once they establish their state funding formula, not in how they allocate the funds among LEAs. Florida and Mississippi allocated funds among their IHEs, including universities and community colleges, using formulas based on factors such as enrollment levels. Other states allocated SFSF funds taking into consideration the budget conditions of the IHEs.

Regarding LEAs, most states planned to allocate funds based on states' primary funding formulae. Many states are using a state formula based on student enrollment weighted by characteristics of students and LEAs. For example, Colorado's formula accounts for the number of students at risk while the formula used by the District allocates funds to LEAs using weights for each student based on the relative cost of educating students with specific characteristics. For example, an official from Washington, D.C. Public Schools said a student who is an English language learner may cost more to educate than a similar student who is fluent in English.

States may use the government services portion of SFSF for education but have discretion to use the funds for a variety of purposes. Officials from Florida, Illinois, New Jersey, and New York reported that their states plan to use some or most of their government services funds for educational purposes. Other states are applying the funds to public safety. For example, according to state officials, California is using the government services fund for its corrections system, and Georgia will use the funds for salaries of state troopers and staff of forensic laboratories and state prisons.

Officials in many school districts told us that SFSF funds would help offset state budget cuts and would be used to maintain current levels of education funding. However, many school district officials also reported that using SFSF funds for education reforms was challenging given the other more pressing fiscal needs.

Although their plans are generally not finalized, officials in many school districts we visited reported that their districts are preparing to use SFSF funds to prevent teacher layoffs, hire new teachers, and provide professional development programs. Most school districts will use the funding to help retain jobs that would have been cut without SFSF funding. For example, Miami Dade officials estimate that the stabilization funds will help them save nearly two thousand teaching positions. State and school district officials in eight states we visited (California, Colorado, Florida, Georgia, Massachusetts, Michigan, New York, and North Carolina)

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also reported that SFSF funding will allow their state to retain positions, including teaching positions that would have been eliminated without the funding. In the Richmond County School System in Georgia, officials noted they plan to retain positions that support its schools, such as teachers, paraprofessionals, nurses, media specialists and guidance counselors. Local officials in Mississippi reported that budget-related hiring freezes had hindered their ability to hire new staff, but because of SFSF funding, they now plan to hire. In addition, local officials in a few states told us they plan to use the funding to support teachers. For example, officials in Waterloo Community and Ottumwa Community School Districts in Iowa as well as officials from Miami-Dade County in Florida cited professional development as a potential use of funding to support teachers.

Although school districts are preventing layoffs and continuing to provide educational services with the SFSF funding, most did not indicate they would use these funds to pursue educational reform. School district officials cited a number of barriers, which include budget shortfalls, lack of guidance from states, and insufficient planning time. In addition to retaining and creating jobs, school districts have considerable flexibility to use these resources over the next 2 years to advance reforms that could have long-term impact. However, a few school district officials reported that addressing reform efforts was not in their capacity when faced with teacher layoffs and deep budget cuts. In Flint, Michigan, officials reported that SFSF funds will be used to cope with budget deficits rather than to advance programs, such as early childhood education or repairing public school facilities. According to the Superintendent of Flint Community Schools, the infrastructure in Flint is deteriorating, and no new school buildings have been built in over 30 years. Flint officials said they would like to use SFSF funds for renovating buildings and other programs, but the SFSF funds are needed to maintain current education programs.

Officials in many school districts we visited reported having inadequate guidance from their state on using SFSF funding, making reform efforts more difficult to pursue. School district officials in most states we visited reported they lacked adequate guidance from their state to plan and report on the use of SFSF funding. Without adequate guidance and time for planning, school district officials told us that preparing for the funds was difficult. At the time of our visits, several school districts were unaware of their funding amounts, which, officials in two school districts said, created additional challenges in planning for the 2009-2010 school year. One charter school we visited in North Carolina reported that layoffs will be required unless their state notifies them soon how much SFSF funding

**IHEs Plan to Use SFSF Funds for Faculty Salaries and Other Purposes and Expect the Funds to Save Jobs and Mitigate Tuition Increases**

they will receive. State officials in North Carolina, as well as in several other states, told us they are waiting for the state legislature to pass the state budget before finalizing SFSF funding amounts for school districts.

Although many IHEs had not finalized plans for using SFSF funds, the most common expected use for the funds at the IHEs we visited was to pay salaries of IHE faculty and staff.<sup>27</sup> Officials at most of the IHEs we visited told us that, due to budget cuts, their institutions would have faced difficult reductions in faculty and staff if they were not receiving SFSF funds. Other IHEs expected to use SFSF funds in the future to pay salaries of certain employees during the year.

Several IHEs we visited are considering other uses for SFSF funds. Officials at the Borough of Manhattan Community College in New York City want to use some of their SFSF funds to buy energy saving light bulbs and to make improvements in the college's very limited space such as, by creating tutoring areas and study lounges. Northwest Mississippi Community College wants to use some of the funds to increase e-learning capacity to serve the institution's rapidly increasing number of students. Several other IHEs plan to use some of the SFSF funds for student financial aid.

Because many IHEs expect to use SFSF funds to pay salaries of current employees that they likely would not have been able to pay without the SFSF funds, IHEs officials said that SFSF funds will save jobs. Officials at several IHEs noted that this will have a positive impact on the educational environment such as, by preventing increases in class size and enabling the institutions to offer the classes that students need to graduate. In addition to preserving existing jobs, some IHEs anticipate creating jobs with SFSF funds. Besides saving and creating jobs at IHEs, officials noted that SFSF monies will have an indirect impact on jobs in the community. IHE officials also noted that SFSF funds will indirectly improve employment because some faculty being paid with the funds will help unemployed workers develop new skills, including skills in fields, such as health care, that have a high demand for trained workers. State and IHE officials also believe that SFSF funds are reducing the size of tuition and fee increases.

<sup>27</sup>During our review, we met with IHEs and state officials responsible for IHE oversight in 8 states—California, Florida, Georgia, Illinois, Mississippi, New York, North Carolina, and Ohio.

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**Other Selected Programs**

Our report provides additional details on the use of Recovery Act funds for these three programs in the 16 selected states and the District. In addition to Medicaid FMAP, Highway Infrastructure Investment, and SFSP, we also reviewed six other programs receiving Recovery Act funds. These programs are:

- Title I, Part A of the Elementary and Secondary Education Act of 1965 (ESEA)
- Parts B and C of the Individuals with Disabilities Education Act (IDEA)
- Workforce Investment Act (WIA) Youth Program
- Public Housing Capital Fund
- Edward Byrne Memorial Justice Assistance Grant (JAG) Program
- Weatherization Assistance Program

Additional detail regarding the states' and localities' use of funds for these programs is available in the full report, GAO-09-829. Individual state summaries for the 16 selected states and the District are accessible through GAO's recovery page at [www.gao.gov/recovery](http://www.gao.gov/recovery) and in an electronic supplement, GAO-09-830SP.

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**Recovery Act Funding Helped States Address Budget Challenges**

State revenue continued to decline and states used Recovery Act funding to reduce some of their planned budget cuts and tax increases to close current and anticipated budget shortfalls for fiscal years 2009 and 2010.<sup>28</sup> Of the 16 states and the District, 15 estimate fiscal year 2009 general fund revenue collections will be less than in the previous fiscal year.<sup>29</sup> For two of the selected states—Iowa and North Carolina—revenues were lower than projected but not less than the previous fiscal year. As shown in figure 3, data from the Bureau of Economic Analysis (BEA) also indicate that the rate of state and local revenue growth has generally declined since

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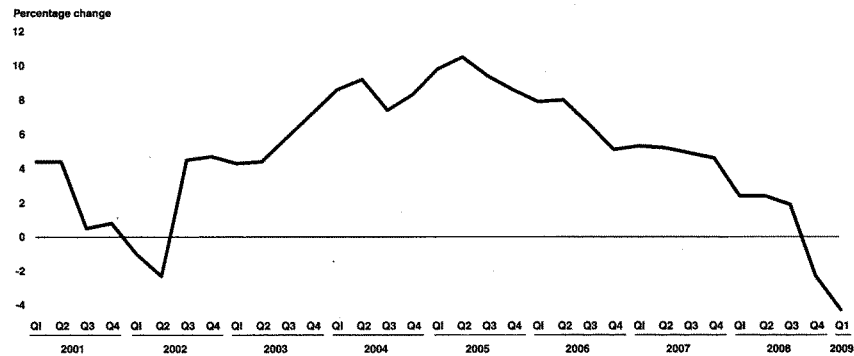
<sup>28</sup>According to the National Association of State Budget Officers (NASBO), most states have balanced-budget requirements for general funds, which may include requirements such as (1) requiring governors to submit a balanced budget, (2) mandating that their legislatures pass a balanced budget, (3) directing governors to sign a balanced budget, or (4) requiring governors to execute a balanced budget. According to NASBO, all of the states we visited have balanced-budget requirements. (In its report, NASBO did not provide information on the District of Columbia's balanced budget requirements.) See NASBO, *Budget Processes in the States* (Washington, D.C.: Summer 2008).

<sup>29</sup>Michigan—along with the District of Columbia—has a fiscal year that begins October 1. New York's fiscal year begins April 1, and the fiscal year for Texas begins on September 1. All other states we visited have fiscal years beginning July 1.



the second quarter of 2005, and the rate of growth has been negative in the fourth quarter of 2008 and the first quarter of 2009.<sup>30</sup>

**Figure 3: Year-Over-Year Change in State and Local Government Current Tax Receipts**



Source: GAO analysis of BEA data.

Officials in most of the selected states and the District expect these revenue trends to contribute to budget gaps (estimated revenues less than estimated disbursements) anticipated for future fiscal years. All of the 16 states and the District forecasted budget gaps in state fiscal year 2009-2010 before budget actions were taken.

Consistent with one of the purposes of the act, states' use of Recovery Act funds to stabilize their budgets helped them minimize and avoid reductions in services as well as tax increases. States took a number of

<sup>30</sup>Recent reports provide additional details regarding revenue declines beyond our selected states. For example, see The National Governors Association and the National Association of State Budget Officers (NASBO), *The Fiscal Survey of States* (Washington, D.C., June 2009); National Conference of State Legislatures, *Budget Update: April 2009* (Washington, D.C., April 2009); Lucy Dadayan and Donald J. Boyd, The Nelson A. Rockefeller Institute of Government, *April is the Cruellest Month: Personal Income Tax Revenues Portend Deepening Trouble for Many States* (Albany, N.Y., June 18, 2009).

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actions to balance their budgets in fiscal year 2009-2010, including staff layoffs, furloughs, and program cuts. The use of Recovery Act funds affected the size and scope of some states' budgeting decisions, and many of the selected states reported they would have had to make further cuts to services and programs without the receipt of Recovery Act funds. For example, California, Colorado, Georgia, Illinois, Massachusetts, Michigan, New York, and Pennsylvania budget officials all stated that current or future budget cuts would have been deeper without the receipt of Recovery Act funds.

Recovery Act funds helped cushion the impact of states' planned budget actions but officials also cautioned that current revenue estimates indicate that additional state actions will be needed to balance future-year budgets. Future actions to stabilize state budgets will require continued awareness of the maintenance-of-effort (MOE) requirements for some federal programs funded by the Recovery Act. For example, Massachusetts officials expressed concerns regarding MOE requirements attached to federal programs, including those funded through the Recovery Act, as future across-the-board spending reductions could pose challenges for maintaining spending levels in these programs. State officials said that MOE requirements that require maintaining spending levels based upon prior-year fixed dollar amounts will pose more of a challenge than upholding spending levels based upon a percentage of program spending relative to total state budget expenditures. In addition, some states also reported accelerating their use of Recovery Act funds to stabilize deteriorating budgets.

Many states, such as Colorado, Florida, Georgia, Iowa, New Jersey, and North Carolina, also reported tapping into their reserve or rainy-day funds in order to balance their budgets. In most cases, the receipt of Recovery Act funds did not prevent the selected states from tapping into their reserve funds, but a few states reported that without the receipt of Recovery Act funds, withdrawals from reserve funds would have been greater.<sup>31</sup> Officials from Georgia stated that although they have already used reserve funds to balance their fiscal year 2009 and 2010 budgets, they may use additional reserve funds if, at the end of fiscal year 2009, revenues are lower than the most recent projections. In contrast, New York officials stated they were able to avoid tapping into the state's reserve funds due to

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<sup>31</sup> According to NASBO, the selected states have varying legal requirements regarding contributions to and withdrawals from various types of reserve funds.

Approaches to Developing Exit Strategies for End of Recovery Act Funding Influenced by Nature of State Budget Processes	<p>the funds made available as a result of the increased Medicaid FMAP funds provided by the Recovery Act.</p> <p>States' approaches to developing exit strategies for the use of Recovery Act funds reflect the balanced-budget requirements in place for all of our selected states and the District. Budget officials referred to the temporary nature of the funds and fiscal challenges expected to extend beyond the timing of funds provided by the Recovery Act. Officials discussed a desire to avoid what they referred to as the "cliff effect" associated with the dates when Recovery Act funding ends for various federal programs.</p> <p>Budget officials in some of the selected states are preparing for the end of Recovery Act funding by using funds for nonrecurring expenditures and hiring limited-term positions to avoid creating long-term liabilities. A few states reported that although they are developing preliminary plans for the phasing out of Recovery Act funds, further planning has been delayed until revenue and expenditure projections are finalized.</p>
<b>States Have Implemented Various Internal Control Programs: However, Single Audit Guidance and Reporting Does Not Adequately Address Recovery Act Risk</b>	<p>Given that Recovery Act funds are to be distributed quickly, effective internal controls over use of funds are critical to help ensure effective and efficient use of resources, compliance with laws and regulations, and in achieving accountability over Recovery Act programs. Internal controls include management and program policies, procedures, and guidance that help ensure effective and efficient use of resources; compliance with laws and regulations; prevention and detection of fraud, waste, and abuse; and the reliability of financial reporting. Management is responsible for the design and implementation of internal controls and the states in our sample have a range of approaches for implementing their internal controls.</p> <p>Some states have internal control requirements in their state statutes and others have undertaken internal control programs as management initiatives. In our sample, 7 states—California, Colorado, Florida, Michigan, Mississippi, New York, and North Carolina—have statutory requirements for internal control programs and activities. An additional 9 states—Arizona, Georgia, Illinois, Iowa, Massachusetts, New Jersey, Ohio, Pennsylvania, and Texas—have undertaken various internal control programs. In addition, the District of Columbia has taken limited actions related to its internal control program. An effective internal control program helps manage change in response to shifting environments and evolving demands and priorities, such as changes related to implementing the Recovery Act.</p>

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Risk assessment and monitoring are key elements of internal controls, and the states in our sample and the District have undertaken a variety of actions in these areas.

- Risk assessment involves performing comprehensive reviews and analyses of program operations to determine if internal and external risks exist and to evaluate the nature and extent of risks which have been identified. Approaches to risk analysis can vary across organizations because of differences in missions and the methodologies used to qualitatively and quantitatively assign risk levels.
- Monitoring activities include the systemic process of reviewing the effectiveness of the operation of the internal control system. These activities are conducted by management, oversight entities, and internal and external auditors. Monitoring enables stakeholders to determine whether the internal control system continues to operate effectively over time. Monitoring also provides information and feedback to the risk assessment process.

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#### Challenges Exist in Tracking Recovery Act Funds

States and localities are responsible for tracking and reporting on Recovery Act funds.<sup>32</sup> OMB has issued guidance to the states and localities that provides for separate identification—"tagging"—of Recovery Act funds so that specific reports can be created and transactions can be specifically identified as Recovery Act funds.<sup>33</sup> The flow of federal funds to the states varies by program, the grantor agencies have varied grants management processes and grants vary substantially in their types, purposes, and administrative requirements.<sup>34</sup>

Several states and the District of Columbia have created unique codes for their financial systems in order to tag the Recovery Act funds. Most state and local program officials told us that they will apply existing controls

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<sup>32</sup>Recovery Act, div. A, title XV, § 1512.

<sup>33</sup>OMB memoranda, M-09-10, *Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, February 18, 2009, and M-09-15, *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009*, April 3, 2009.

<sup>34</sup>GAO, *Grants Management: Additional Actions Needed to Streamline and Simplify Process*, GAO-05-335 (Washington, D.C.: April 2005).

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and oversight processes that they currently apply to other program funds to oversee Recovery Act funds.

In addition to being an important accountability mechanism, audit results can provide valuable information for use in management's risk assessment and monitoring processes. The single audit report, prepared to meet the requirements of the Single Audit Act,<sup>35</sup> as amended (Single Audit Act), is a source of information on internal control and compliance findings and the underlying causes and risks. The report is prepared in accordance with OMB's implementing guidance in OMB Circular No. A-133, *Audits of States, Local Governments, and Non-Profit Organizations*,<sup>36</sup> which provides guidance to auditors on selecting federal programs for audit and the related internal control and compliance audit procedures to be performed.

In our April 23, 2009 report, we reported that the guidance and criteria in OMB Circular No. A-133 do not adequately address the substantial added risks posed by the new Recovery Act funding. Such risks may result from (1) new government programs, (2) the sudden increase in funds or programs that are new to the recipient entity, and (3) the expectation that some programs and projects will be delivered faster so as to inject funds into the economy. With some adjustment, the single audit could be an effective oversight tool for Recovery Act programs, addressing risks associated with all three of these factors.

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<sup>35</sup>The Single Audit Act requires states, local governments, and nonprofit organizations expending over \$500,000 in federal awards in a year to obtain an audit in accordance with requirements set forth in the Act. A single audit consists of (1) an audit and opinions on the fair presentation of the financial statements and the Schedule of Expenditures of Federal Awards; (2) gaining an understanding of and testing internal control over financial reporting and the entity's compliance with laws, regulations, and contract or grant provisions that have a direct and material effect on certain federal programs (i.e., the program requirements); and (3) an audit and an opinion on compliance with applicable program requirements for certain federal programs.

<sup>36</sup>The auditor identifies the applicable federal programs, including "major programs," based on risk criteria, including minimum dollar thresholds, set out in the Single Audit Act and OMB Circular No. A-133. Guidance on identifying compliance requirements for most large federal programs is set out in the Compliance Supplement to OMB Circular No. A-133. OMB has 14 requirements that generally are to be tested for each major federal program to opine on compliance and report on significant deficiencies in internal control over compliance with each applicable compliance requirement.

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Our April 2009 report on the Recovery Act included recommendations that OMB adjust the current audit process to:

- focus the risk assessment auditors use to select programs to test for compliance with 2009 federal program requirements on Recovery Act funding;
- provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010; and
- evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.

Since April, although OMB has taken several steps in response to our recommendations, these actions do not sufficiently address the risks leading to our recommendations. To focus auditor risk assessments on Recovery Act-funded programs and to provide guidance on internal control reviews for Recovery Act programs, OMB is working within the framework defined by existing mechanisms—Circular No. A-133 and the Compliance Supplement. In this context, OMB has made limited adjustments to its single audit guidance and is planning to issue additional guidance later this month.

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**Focusing Auditors’  
Program Risk Assessments  
on Programs with  
Recovery Act Funding**

On May 26, OMB issued the 2009 edition of the Circular A-133 Compliance Supplement. The new Compliance Supplement is intended to focus auditor risk assessment on Recovery Act funding by, among things (1) requiring that auditors specifically ask auditees about and be alert to expenditure of funds provided by the Recovery Act, and (2) providing an appendix that highlights some areas of the Recovery Act impacting single audits. The appendix adds a requirement that large programs and program clusters with Recovery Act funding cannot be assessed as low-risk for the purposes of program selection without clear documentation of the reasons they are considered low risk. It also calls for recipients to separately identify expenditures for Recovery Act programs on the Schedule of Expenditures of Federal Awards.

OMB issued Compliance Supplement Addendum No. 1 on August 6, 2009 to provide additional guidance for programs (including clusters of programs with expenditures of Recovery Act funds). This addendum modifies the 2009 Compliance Supplement by indicating the new Recovery Act programs and new program clusters, providing new cross-cutting provisions related to the Recovery Act programs, and adding additional

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compliance requirements for existing programs as a result of Recovery Act funding.

OMB Circular A-133 relies heavily on the amount of federal expenditures in a program during a fiscal year and whether findings were reported in the previous period to determine whether detailed compliance testing is required for that year. Although OMB is using clusters for single audit selection to make it more likely that Recovery Act programs would be selected as major programs subject to internal control and compliance testing, the dollar formulas for determining major programs have not changed. This approach may not provide sufficient assurance that smaller, but nonetheless significant, Recovery Act-funded programs would be selected for audit.

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**Steps Toward More Timely  
Reporting on Internal  
Controls over Recovery  
Act-funded Programs**

To provide additional focus on internal control reviews, OMB issued guidance in early August that emphasizes the importance of prompt corrective action by management. This guidance also encourages early communication by auditors to management and those charged with governance of identified control deficiencies related to Recovery Act funding that are, or are likely to be, significant deficiencies or material weaknesses. Such early communication is intended to allow management to expedite corrective action and mitigate the risk of improper expenditure of federal awards.

In our July report, we stated that OMB was encouraging communication of weaknesses to management early in the audit process, but did not add requirements for auditors to take these steps. This step was insufficient and did not address our concern that internal controls over Recovery Act programs should be reviewed before significant funding is expended. Under the current single audit framework and reporting timelines, the auditor evaluation of internal control and related reporting will occur too late—after significant levels of federal expenditures have already occurred.

OMB is currently vetting a proposed pilot project under which a limited number of voluntarily participating auditors performing the single audits for states would communicate in writing internal control deficiencies noted in the single audit within six months of the 2009 fiscal year-end, rather than the nine months required by the Single Audit Act. As currently envisioned, an auditor participating in the pilot would report internal control deficiencies identified in the course of the single audit to state and federal officials within six months of the end of the audited entity's fiscal

year in order to achieve more timely accountability for selected Recovery Act-funded programs. Most states have a June 30 fiscal year-end; consequently most of the preliminary internal control communications would be due by December 31, 2009. Participating auditors would be required to focus audit procedures on Recovery Act-funded programs in accordance with guidelines prescribed by OMB. OMB would offer to waive Circular A-133's requirement for risk assessment for smaller programs as an inducement to participate. OMB is moving ahead with the pilot and plans to identify the participating auditors and the programs that will be included by the end of September 2009. GAO believes that, if the pilot is properly implemented and achieves sufficient coverage of Recovery Act-funded programs, it may be effective in addressing concerns about the timeliness of single audit reporting related to internal control weaknesses in Recovery Act programs. The pilot is, however, still in its early stages and many surrounding issues are yet to be resolved. It is important to note that the pilot project is dependent on voluntary participation, which could impact OMB's ability to achieve sufficient scope and coverage for the project to meet its objectives.

**Providing relief to Balance  
Expected Increased  
Workload**

While OMB has noted the increased responsibilities falling on those responsible for performing single audits, it has not issued any proposals or plans to address this recommendation to date. A recent survey conducted by the staff of the National State Auditors' Association (NSAA)<sup>37</sup> highlighted the need for relief to over-burdened state audit organizations that have experienced staffing reductions and furloughs.

In addition, states volunteering to participate in OMB's proposed pilot program will be granted some relief in the workload because the auditor will not be required to perform risk assessments of smaller federal programs. Auditors conduct these risk assessments as part of the planning process to identify which federal programs will be subject to detailed internal control and compliance testing. We believe that this step alone will not provide sufficient relief to balance out additional audit requirements for Recovery Act programs. Without action now audit coverage of Recovery Act programs will not be sufficient to address Recovery Act risks and the audit reporting that does occur will be after significant expenditures have already occurred.

<sup>37</sup>NSAA's mission is to unite state auditors by encouraging and providing opportunities for the free exchange of information and ideas between auditors on the state, federal and local levels.



Congress is considering a bill that could provide some financial relief to auditors lacking the staff capacity necessary to handle the increased audit responsibilities associated with the Recovery Act. S. 1064 which is currently before this Committee and its companion bill that was passed by the House, H.R. 2182, would amend the Recovery Act to provide for enhanced state and local oversight of activities conducted pursuant to the Act. One key provision of the legislation would allow state and local governments to set aside 0.5 percent of Recovery Act funds, in addition to funds already allocated to administrative expenditures, to conduct planning and oversight. We support these efforts to provide financial support to auditors to meet their responsibilities associated with the Recovery Act. This Committee should be commended for its leadership on this matter.

**Single Audit Reporting Will  
Not Facilitate Timely  
Reporting of Recovery Act  
Program Findings and  
Risks**

The single audit reporting deadline is too late to provide audit results in time for the audited entity to take action on deficiencies noted in Recovery Act programs. The Single Audit Act requires that recipients submit their Single Audit reports to the federal government no later than nine months after the end of the period being audited.<sup>38</sup> As a result an audited entity may not receive feedback needed to correct an identified internal control or compliance weakness until the latter part of the subsequent fiscal year. For example, states that have a fiscal year end of June 30th have a reporting deadline of March 31st, which leaves program management only 3 months to take corrective action on any audit findings before the end of the subsequent fiscal year. For Recovery Act programs, significant expenditure of funds could occur during the period prior to the audit report being issued.

The timing problem is exacerbated by the extensions to the 9 month deadline that are routinely granted by the awarding agencies, consistent with OMB guidance. For example, 13 of the 17 states in our sample have a June 30 fiscal year end and 7 of these 13 states requested and received extensions for their March 31, 2009 submission requirement of their fiscal

<sup>38</sup>Single Audit Act Section 7502(b)(2). The guidance provides that under certain conditions, Single Audit auditees may be audited biennially instead of annually. For entities that are audited biennially, it is longer before internal control and compliance weaknesses are identified and remediated.

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year 2008 reporting package.<sup>36</sup> The Health and Human Services Office of Inspector General (HHS OIG) is the cognizant agency for most of the states, including all of the states selected for review under the Recovery Act. According to a HHS OIG official, beginning in May 2009 HHS IG adopted a policy of no longer approving requests for extensions of the due dates for single audit reporting package submissions. OMB officials have stated that they plan to eliminate allowing extensions of the reporting package, but have not issued any official guidance or memorandum to the agencies, OIGs, or federal award recipients.

In order to realize the single audit's full potential as an effective Recovery Act oversight tool, OMB needs to take additional action to focus auditors' efforts on areas that can provide the most efficient, and most timely, results. As federal funding of Recovery Act programs accelerates in the next few months, we are particularly concerned that the Single Audit process may not provide the timely accountability and focus needed to assist recipients in making necessary adjustments to internal controls so that they achieve sufficient strength and capacity to provide assurances that the money is being spent as effectively as possible to meet program objectives.

As discussed in the previous section, OMB is currently vetting a proposed pilot project under which a limited number of voluntarily participating auditors performing the single audits for states would communicate in writing internal control deficiencies noted in the single audit within six months of the 2009 fiscal year-end, rather than the nine months required by the Single Audit Act. If the pilot is properly implemented and achieves sufficient coverage of Recovery Act-funded programs, it may be effective in addressing concerns about the timeliness of single audit reporting related to internal control weaknesses in Recovery Act programs.

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<sup>36</sup>Department of Health and Human Services is the cognizant agency for the 16 states and District of Columbia that are included in our study. According to OMB Circular No. A-133 §.400(a)(2), if an entity needs an extension for submission of their single audit report, the cognizant agency must consider auditee requests for extension to the report submission due date.

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**GAO's Review of  
Allegations of Fraud,  
Waste, and Abuse  
Submitted to FraudNet**

As of September 2, 2009, GAO's FraudNet has received 80 Recovery Act-related allegations that were considered credible enough to warrant further review. Our Forensic Audits and Special Investigations unit is pursuing 8 of these allegations, which include wasteful and improper spending, conflicts of interest, supplanting of Recovery Act funds, and contract fraud. Of the remaining 72 allegations, 12 are pending further review by GAO criminal investigators and 38 were found to not address waste, fraud, or abuse; lacked specificity; were not Recovery Act-related; or reflected only a disagreement with how Recovery Act funds are being disbursed. We consider these allegations to be resolved and no further investigation is necessary. An additional 22 allegations were referred to the appropriate agency Inspectors General for further review and investigation. We will continue to monitor these referrals and will inform the Committee when outstanding allegations are resolved.

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**Efforts to Assess the  
Impact of Recovery  
Act Spending**

As recipients of Recovery Act funds and as partners with the federal government in achieving Recovery Act goals, states and local units of government are expected to invest Recovery Act funds with a high level of transparency and to be held accountable for results under the Recovery Act. Under the Recovery Act, direct recipients of the funds, including states and localities, are expected to report quarterly on a number of measures including the use of funds and an estimate of the number of jobs created and the number of jobs retained. These measures are part of the recipient reports required under section 1512(c) of the Recovery Act and will be submitted by recipients starting in October 2009. OMB guidance described recipient reporting requirements under the Recovery Act's section 1512 as the minimum performance measures that must be collected, leaving it to federal agencies to determine additional information that would be required for oversight of individual programs funded by the Recovery Act, such as the Department of Energy Weatherization Assistance Program and the Department of Justice Edward Byrne Memorial Justice Assistance Grant (JAG) Program.

In general, states are adapting information systems, issuing guidance, and beginning to collect data on jobs created and jobs retained, but questions remained about how to count jobs and measure performance under Recovery Act-funded programs. Over the last several months OMB met regularly with state and local officials, federal agencies, and others to gather input on the reporting requirements and implementation guidance. OMB also worked with the Recovery Accountability and Transparency Board to design a nationwide data collection system that will reduce information reporting burdens on recipients by simplifying reporting

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instructions and providing a user-friendly mechanism for submitting required data. OMB will be testing this system in July.

In response to requests for more guidance on the recipient reporting process and required data, OMB, after soliciting responses from an array of stakeholders, issued additional implementing guidance for recipient reporting on June 22, 2009.<sup>40</sup> In addition to other areas, the new OMB guidance clarifies that recipients of Recovery Act funds are required to report only on jobs directly created or retained by Recovery Act-funded projects, activities, and contracts. Recipients are not expected to report on the employment impact on materials suppliers ("indirect" jobs) or on the local community ("induced" jobs). The OMB guidance also provides additional instruction on estimating the number of jobs created and retained by Recovery Act funding. OMB's guidance on the implementation of recipient reporting should be helpful in addressing answers to many of the questions and concerns raised by state and local program officials. However, federal agencies may need to do a better job of communicating the OMB guidance in a timely manner to their state counterparts and, as appropriate, issue clarifying guidance on required performance measurement.

OMB's guidance for reporting on job creation aims to shed light on the immediate uses of Recovery Act funding; however, reports from recipients of Recovery Act funds must be interpreted with care. For example, accurate, consistent reports will only reflect a portion of the likely impact of the Recovery Act on national employment, since Recovery Act resources are also made available through tax cuts and benefit payments.<sup>41</sup> OMB noted that a broader view of the overall employment impact of the Recovery Act will be covered in the estimates generated by the Council of Economic Advisers (CEA) using a macro-economic approach. According to CEA, it will consider the direct jobs created and retained reported by recipients to supplement its analysis.<sup>42</sup>

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<sup>40</sup>OMB memoranda, M-09-21, *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009* (June 22, 2009).

<sup>41</sup>The recipient reporting requirement only covers a defined subset of the Recovery Act's funding. The reporting requirements apply to recipients who receive funding through discretionary appropriations, not recipients receiving funds through entitlement programs, such as Medicaid, or tax programs. Recipient reporting also does not apply to individuals.

<sup>42</sup>Executive Office of the President, Council of Economic Advisers, *Estimates of Job Creation From the American Recovery and Reinvestment Act of 2009* (May 2009).

## Concluding Observations and Recommendations

Since enactment of the Recovery Act in February 2009, OMB has issued three sets of guidance—on February 18, April 3 and, most recently, June 22, 2009<sup>46</sup>—to, among other things, assist recipients of federal Recovery Act funds in complying with reporting requirements. OMB has reached out to Congress, federal, state, and local government officials, grant and contract recipients, and the accountability community to get a broad perspective on what is needed to meet the high expectations set by Congress and the administration. Further, according to OMB's June guidance they have worked with the Recovery Accountability and Transparency Board to deploy a nationwide data collection system at [www.federalreporting.gov](http://www.federalreporting.gov).

As work proceeds on the implementation of the Recovery Act, OMB and the cognizant federal agencies have opportunities to build on the early efforts by continuing to address several important issues.

These issues can be placed broadly into three categories, which have been revised from our last report to better reflect evolving events since April: (1) accountability and transparency requirements, (2) reporting on impact, and (3) communications and guidance.

## Accountability and Transparency Requirements

Recipients of Recovery Act funding face a number of implementation challenges in this area. The act includes new programs and significant increases in funds out of normal cycles and processes. There is an expectation that many programs and projects will be delivered faster so as to inject funds into the economy, and the administration has indicated its intent to assure transparency and accountability over the use of Recovery Act funds. Issues regarding the Single Audit process and administrative support and oversight are important.

**Single Audit:** The Single Audit process needs adjustments to provide appropriate risk-based focus and the necessary level of accountability over Recovery Act programs in a timely manner.

<sup>46</sup>OMB Memorandum M-09-15, *Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009* (Apr. 3, 2009). This guidance supplements, amends, and clarifies the initial guidance issued by OMB on February 18, 2009. OMB memoranda, M-09-21, *Implementing Guidance for the Reports on Use of Funds Pursuant to the American Recovery and Reinvestment Act of 2009* (June 22, 2009).

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In our April 2009 report, we reported that the guidance and criteria in OMB Circular No. A-133 do not adequately address the substantial added risks posed by the new Recovery Act funding. Such risks may result from (1) new government programs, (2) the sudden increase in funds or programs that are new to the recipient entity, and (3) the expectation that some programs and projects will be delivered faster so as to inject funds into the economy. With some adjustment, the Single Audit could be an effective oversight tool for Recovery Act programs because it can address risks associated with all three of these factors.

**April report recommendations:** Our April report included recommendations that OMB adjust the current audit process to focus the risk assessment auditors use to select programs to test for compliance with 2009 federal program requirements on Recovery Act funding; provide for review of the design of internal controls during 2009 over programs to receive Recovery Act funding, before significant expenditures in 2010; and evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.

**Status of April report recommendations:** OMB has taken some actions and has other planned actions to help focus the program selection risk assessment on Recovery Act programs and to provide guidance on auditors' reviews of internal controls for those programs. However, we remain concerned that OMB's planned actions would not achieve the level of accountability needed to effectively respond to Recovery Act risks and does not provide for timely reporting on internal controls for Recovery Act programs. Therefore, in our July report, we re-emphasized our previous recommendations in this area.

To help auditors with single audit responsibilities meet the increased demands imposed on them by Recovery Act funding, we recommend that the Director of OMB take the following four actions:

- Consider developing requirements for reporting on internal controls during 2009 before significant Recovery Act expenditures occur as well as ongoing reporting after the initial report.
- Provide more focus on Recovery Act programs through the Single Audit to help ensure that smaller programs with high risk have audit coverage in the area of internal controls and compliance.

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- Evaluate options for providing relief related to audit requirements for low-risk programs to balance new audit responsibilities associated with the Recovery Act.
  - To the extent that options for auditor relief are not provided, develop mechanisms to help fund the additional Single Audit costs and efforts for auditing Recovery Act programs.

**Status of Recommendations:** OMB is currently vetting a proposed pilot project under which a limited number of voluntarily participating auditors performing the single audits for states would communicate in writing internal control deficiencies noted in the single audit within six months of the 2009 fiscal year-end, rather than the nine months required by the Single Audit Act. If the pilot is properly implemented and achieves sufficient coverage of Recovery Act-funded programs, it may be effective in addressing concerns about the timeliness of single audit reporting related to internal control weaknesses in Recovery Act programs. Because the sufficiency of scope and coverage from this pilot program is uncertain, we are making an additional recommendation to OMB.

**September recommendation:** In order to achieve the objective of more timely reporting of internal control deficiencies over Recovery Act programs, the Director of OMB should take steps to achieve sufficient participation and coverage in the single audit pilot program that provides for early written communication of internal control deficiencies.

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#### Matter for Congressional Consideration

Because a significant portion of Recovery Act expenditures will be in the form of federal grants and awards, the Single Audit process could be used as a key accountability tool over these funds. However, the Single Audit Act, enacted in 1984 and most recently amended in 1996, did not contemplate the risks associated with the current environment where large amounts of federal awards are being expended quickly through new programs, greatly expanded programs, and existing programs. The current Single Audit process is largely driven by the amount of federal funds expended by a recipient in order to determine which federal programs are subject to compliance and internal control testing. Not only does this model potentially miss smaller programs with high risk, but it also relies on audit reporting 9 months after the end of a grantee's fiscal year—far too late to preemptively correct deficiencies and weaknesses before significant expenditures of federal funds. Congress is considering a legislative proposal in this area and could address the following issues:

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- To the extent that appropriate adjustments to the Single Audit process are not accomplished under the current Single Audit structure, Congress should consider amending the Single Audit Act or enacting new legislation that provides for more timely internal control reporting, as well as audit coverage for smaller Recovery Act programs with high risk.
  - To the extent that additional audit coverage is needed to achieve accountability over Recovery Act programs, Congress should consider mechanisms to provide additional resources to support those charged with carrying out the Single Audit act and related audits.
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#### Administrative Support and Oversight

States have been concerned about the burden imposed by new requirements, increased accounting and management workloads, and strains on information systems and staff capacity at a time when they are under severe budgetary stress.

**April report recommendation:** In our April report, we recommended that the director of OMB clarify what Recovery Act funds can be used to support state efforts to ensure accountability and oversight, especially in light of enhanced oversight and coordination requirements.

- **Status of April report recommendation:** On May 11, 2009, OMB released a memorandum<sup>4</sup> clarifying how state grantees could recover administrative costs of Recovery Act activities.

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#### Reporting on Impact

Under the Recovery Act, responsibility for reporting on jobs created and retained falls to nonfederal recipients of Recovery Act funds. As such, states and localities have a critical role in identifying the degree to which Recovery Act goals are achieved.

Performance reporting is broader than the jobs reporting required under section 1512 of the Recovery Act. OMB guidance requires that agencies collect and report performance information consistent with the agency's program performance measures. As described earlier in this report, some agencies have imposed additional performance measures on projects or activities funded through the Recovery Act.

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<sup>4</sup>OMB memoranda, M-09-18, *Payments to State Grantees for Administrative Costs of Recovery Act Activities* (May 11, 2009).



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**April report recommendation:** In our April report, we recommended that given questions raised by many state and local officials about how best to determine both direct and indirect jobs created and retained under the Recovery Act, the Director of OMB should continue OMB's efforts to identify appropriate methodologies that can be used to (1) assess jobs created and retained from projects funded by the Recovery Act; (2) determine the impact of Recovery Act spending when job creation is indirect; (3) identify those types of programs, projects, or activities that in the past have demonstrated substantial job creation or are considered likely to do so in the future and consider whether the approaches taken to estimate jobs created and jobs retained in these cases can be replicated or adapted to other programs.

**Status of April report recommendation:** OMB has been meeting on a regular basis with state and local officials, federal agencies, and others to gather input on reporting requirements and implementation guidance and has worked with the Recovery Accountability and Transparency Board on a nationwide data collection system. On June 22, OMB issued additional implementation guidance on recipient reporting of jobs created and retained. This guidance is responsive to much of what we said in our April report. It states that there are two different types of jobs reports under the Recovery Act and clarifies that recipient reports are to cover only direct jobs created or retained. "Indirect" jobs (employment impact on suppliers) and "induced" jobs (employment impact on communities) will be covered in Council of Economic Advisers (CEA) quarterly reports on employment, economic growth, and other key economic indicators. Consistent with the statutory language of the act, OMB's guidance states that these recipient reporting requirements apply to recipients who receive funding through discretionary appropriations, not to those receiving funds through either entitlement or tax programs or to individuals. It clarifies that the prime recipient and not the subrecipient is responsible for reporting section 1512 information on jobs created or retained. The June 2009 guidance also provides detailed instructions on how to calculate and report jobs as full-time equivalents (FTE). It also describes in detail the data model and reporting system to be used for the required recipient reporting on jobs.

The guidance provided for reporting job creation aims to shed light on the immediate uses of Recovery Act funding and is reasonable in that context. It will be important, however, to interpret the recipient reports with care. As noted in the guidance, these reports are only one of the two distinct types of reports seeking to describe the jobs impact of the Recovery Act. CEA's quarterly reports will cover the impact on employment, economic growth, and other key economic indicators. Further, the recipient reports

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will not reflect the impact of resources made available through tax provisions or entitlement programs.<sup>45</sup>

Recipients are required to report no later than 10 days after the end of the calendar quarter. The first of these reports is due on October 10, 2009. After prime recipients and federal agencies perform data quality checks, detailed recipient reports are to be made available to the public no later than 30 days after the end of the quarter. Initial summary statistics will be available on [www.recovery.gov](http://www.recovery.gov). The guidance explicitly does not mandate a specific methodology for conducting quality reviews. Rather, federal agencies are directed to coordinate the application of definitions of material omission and significant reporting error to "ensure consistency" in the conduct of data quality reviews. Although recipients and federal agency reviewers are required to perform data quality checks, none are required to certify or approve data for publication. It is unclear how any issues identified under data quality reviews would be resolved and how frequently data quality problems would have been identified in the reviews. We will continue to monitor this data quality and recipient reporting requirements.

**July report recommendations:** To increase consistency in recipient reporting or jobs created and retained, the Director of OMB should work with federal agencies to have them provide program-specific examples of the application of OMB's guidance on recipient reporting of jobs created and retained. This would be especially helpful for programs that have not previously tracked and reported such metrics.

Because performance reporting is broader than the jobs reporting required by section 1512, the Director of OMB should also work with federal agencies—perhaps through the Senior Management Councils—to clarify what new or existing program performance measures—in addition to jobs

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<sup>45</sup>Consistent with GAO's past work showing that tax expenditures receive less scrutiny than outlay programs (e.g., GAO, *Government Performance and Accountability: Tax Expenditures Represent a Substantial Federal Commitment and Need to Be Reexamined*, GAO-05-690 (Washington, D.C.: Sept. 23, 2005), we have begun work to determine the level of transparency and oversight that will be provided for the Recovery Act tax provisions. Administration officials are formulating plans for what information will be collected, analyzed, and reported for the tax provisions. See also: GAO, *American Recovery and Reinvestment Act: GAO's Role in Helping to Ensure Accountability and Transparency*, GAO-09-453T (Washington, D.C.: Mar. 5, 2009).

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created and retained—that recipients should collect and report in order to demonstrate the impact of Recovery Act funding.<sup>46</sup>

In addition to providing these additional types of program-specific examples of guidance, the Director of OMB should work with federal agencies to use other channels to educate state and local program officials on reporting requirements, such as Web- or telephone-based information sessions or other forums.

**Status of July report recommendations:** In recent weeks, federal agencies have issued additional guidance that builds on the OMB June 22nd recipient reporting guidance for their specific programs. This guidance is in the form of frequently asked questions (FAQs), tip sheets, and more traditional guidance that builds on what was provided on June 22. We have not assessed the sufficiency of this additional guidance at this time. Federal agencies have also taken steps to provide additional education and training opportunities for state and local program officials on recipient reporting including web-based seminars.

In addition to the federal agency efforts, OMB has issued clarifications and FAQs on Recovery Act reporting requirements. OMB is also preparing to deploy regional federal employees to serve as liaisons to state and local recipients in large population centers. The objective is to provide onsite assistance and to direct questions to the appropriate federal official. OMB is also establishing a call center for entities that do not have an on-site federal liaison.

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## Communications and Guidance

**Funding notification and program guidance:** State officials expressed concerns regarding communication on the release of Recovery Act funds and their inability to determine when to expect federal agency program guidance. Once funds are released there is no easily accessible, real-time procedure for ensuring that appropriate officials in states and localities

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<sup>46</sup>According to OMB guidance, rather than establishing a new council, agencies are encouraged to leverage their existing Senior Management Councils to oversee Recovery Act performance across the agency, including risk management. The Senior Management Council should be composed of the Chief Financial Officer, Senior Procurement Executive, Chief Human Capital Officer, Chief Information Officer, Performance Improvement Officer, and managers of programmatic offices. The agency's Senior Accountable Official should also participate and assume a leadership role. Agencies should also consider having their Office of General Counsel and Office of Inspectors General serve in advisory roles on the Senior Management Council.

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are notified. Because half of the estimated spending programs in the Recovery Act will be administered by nonfederal entities, states wish to be notified when funds are made available to them for their use as well as when funding is received by other recipients within their state that are not state agencies.

OMB does not have a master timeline for issuing federal agency guidance. OMB's preferred approach is to issue guidance incrementally. This approach potentially produces a more timely response and allows for mid-course corrections; however, this approach also creates uncertainty among state and local recipients responsible for implementing programs. We continue to believe that OMB can strike a better balance between developing timely and responsive guidance and providing a longer range time line that gives some structure to states' and localities' planning efforts.

**April report recommendation:** In our April report, we recommended that to foster timely and efficient communications, the Director of OMB should develop an approach that provides dependable notification to (1) prime recipients in states and localities when funds are made available for their use, (2) states—where the state is not the primary recipient of funds but has a statewide interest in this information—and (3) all nonfederal recipients on planned releases of federal agency guidance and, if known, whether additional guidance or modifications are recommended.

**Status of April recommendation:** OMB has made important progress in the type and level of information provided in its reports on Recovery.gov. Nonetheless, OMB has additional opportunities to more fully address the recommendations we made in April. By providing a standard format across disparate programs, OMB has improved its Funding Notification reports, making it easier for the public to track when funds become available. Since we issued our July report, OMB has announced that beginning August 28, OMB expects federal agencies to notify recovery coordinators in states, the District of Columbia, Commonwealths, and Territories within 48 hours of an award to a grantee or contractor in their jurisdiction. OMB has taken the additional step of disaggregating financial information, i.e., federal obligations and outlays by Recovery Act programs and by state in its Weekly Financial Activity Report. Both reports, along with agency contract and grant awardee information by location, are available on [www.recovery.gov](http://www.recovery.gov).

**Our recommendation:** The Director of OMB should continue to implement OMB's approach to providing easily accessible, real-time

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notification to (1) prime recipients in states and localities when funds are made available for their use, and (2) states—where the state is not the primary recipient of funds but has a statewide interest in this information. In addition, OMB should provide a long range time line for the release of federal guidance for the benefit of nonfederal recipients responsible for implementing Recovery Act programs.

**Recipient financial tracking and reporting guidance:** In addition to employment related reporting, OMB's guidance calls for the tracking of funds by the prime recipient, recipient vendors, and subrecipients receiving payments. OMB's guidance also allows that "prime recipients may delegate certain reporting requirements to subrecipients." Either the prime or sub-recipient must report the D-U-N-S number (or an acceptable alternative) for any vendor or sub-recipient receiving payments greater than \$25 thousand. In addition, the prime recipient must report what was purchased and the amount, and a total number and amount for sub-awards of less than \$25 thousand. By reporting the DUNS number, OMB guidance provides a way to identify subrecipients by project, but this alone does not ensure data quality.

The approach to tracking funds is generally consistent with the Federal Funding Accountability and Transparency Act (FFATA). Like the Recovery Act, the FFATA requires a publicly available Web site—USAspending.gov—to report financial information about entities awarded federal funds. Yet, significant questions have been raised about the reliability of the data on USAspending.gov, primarily because what is reported by the prime recipients is dependent on the unknown data quality and reporting capabilities of their subrecipients.

For example, earlier this year, more than 2 years after passage of FFATA, the Congressional Research Services (CRS) questioned the reliability of the data on USAspending.gov. We share CRS's concerns associated with USAspending.gov, including incomplete, inaccurate, and other data quality problems. More broadly, these concerns also pertain to recipient financial reporting in accordance with the Recovery Act and its federal reporting vehicle, www.FederalReporting.gov, currently under development.

**Our recommendation:** To strengthen the effort to track the use of funds, the Director of OMB should (1) clarify what constitutes appropriate quality control and reconciliation by prime recipients, especially for subrecipient data, and (2) specify who should best provide formal certification and approval of the data reported.

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**Agency-specific guidance:** DOT and FHWA have yet to provide clear guidance regarding how states are to implement the Recovery Act requirement that economically distressed areas are to receive priority in the selection of highway projects for funding. We found substantial variation both in how states identified areas in economic distress and how they prioritized project selection for these areas. As a result, it is not clear whether areas most in need are receiving priority in the selection of highway infrastructure projects, as Congress intended. While it is true that states have discretion in selecting and prioritizing projects, it is also important that this goal of the Recovery Act be met.

**Our recommendation:** To ensure states meet Congress's direction to give areas with the greatest need priority in project selection, the Secretary of Transportation should develop clear guidance on identifying and giving priority to economically distressed areas that are in accordance with the requirements of the Recovery Act and the Public Works and Economic Development Act of 1965, as amended, and more consistent procedures for the Federal Highway Administration to use in reviewing and approving states' criteria.

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## Agency Comments and Our Evaluation

We received comments on a draft of our July report from the U.S. Office of Management and Budget (OMB) and the U.S. Department of Transportation (DOT) on our report recommendations.

**U.S. Office of Management and Budget:** OMB concurs with the overall objectives of our recommendations made to OMB in our report. OMB offered clarifications regarding the area of Single Audit and did not concur with some of our conclusions related to communications. What follows summarizes OMB's comments and our responses.

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## Single Audit Act

OMB agreed with the overall objectives of our recommendations. OMB also noted it believes that new requirements for more rigorous internal control reviews will yield important short-term benefits and the steps taken by state and local recipients to immediately initiate controls will withstand increased scrutiny later in the process. OMB is vetting a proposed pilot project under which a limited number of voluntarily participating auditors performing the single audits for states would communicate in writing internal control deficiencies noted in the single audit within six months of the 2009 fiscal year-end, rather than the nine months as required by the Single Audit Act. In recent discussions about the pilot program, OMB officials agreed that sufficient coverage of

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Recovery Act-funded programs will be needed to address concerns about the timeliness of single audit reporting related to internal control weaknesses in Recovery Act programs.

OMB commented that it has already taken and is planning actions to focus program selection risk assessment on Recovery Act programs and to increase the rigor of state and local internal controls on Recovery Act activities. OMB issued guidance in early August 2009 that provides additional guidance for programs with expenditures of Recovery Act funds. OMB has taken steps to achieve audit coverage of Recovery Act programs. However, smaller, but significantly risky programs under the Recovery Act may not receive adequate attention and scrutiny under the current Single Audit process.

OMB acknowledged that acceleration of internal control reviews could cause more work for state auditors, for which OMB and Congress should explore potential options for relief. States volunteering to participate in OMB's proposed pilot program will be granted some relief in workload because the auditor will not be required to perform risk assessments of smaller federal programs.

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## Communications

OMB has made important progress relative to some communications. In particular, we agree with OMB's statements that it requires agencies to post guidance and funding information to agency Recovery Act websites, disseminates guidance broadly, and seeks out and responds to stakeholder input. In addition, OMB has held a series of interactive forums to offer training and information to Recovery Act recipients on the process and mechanics of recipient reporting and they could also serve as a vehicle for additional communication. Finally OMB has improved Funding Notification reports by providing a standard format across disparate programs, making it easier for the public to track when funds become available. OMB recently established an approach for notifying key state officials no later than 48 hours after an award is made within their state. Although it is too soon to tell, this latest effort may provide the real-time notification we recommend. We will continue to monitor the situation and will report on the effectiveness of OMB's approach in a future report.

Moving forward and building on the progress it has made, OMB can take the following additional step to provide a long range time line for the release of federal agency guidance. In an attempt to be responsive to emerging issues and questions from the recipient community, OMB's preferred approach is to issue guidance incrementally. Since our July

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report, OMB has issued periodic FAQs as an approach to clarifying existing OMB guidance and providing additional information. This approach potentially produces a more timely response and allows for mid-course corrections; however, this approach also creates uncertainty among state and local recipients. State and local officials expressed concerns that this incremental approach hinders their efforts to plan and administer Recovery Act programs. As a result, we continue to believe OMB can strike a better balance between developing timely and responsive guidance, such as its FAQs, and providing some degree of a longer range time line so that states and localities can better anticipate which programs will be affected and when new federal agency guidance is likely to be issued. OMB's consideration of a master schedule and its acknowledgement of the extraordinary proliferation of program guidance in response to Recovery Act requirements seem to support a more structured approach. We appreciate that a longer range time line would need to be flexible so that OMB and federal agencies could also continue to issue guidance and clarifications in a timely manner as new issues and questions emerge.

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Mr. Chairman, Senator Collins, and Members of the Committee this concludes my statement. I would be pleased to respond to any questions you may have.

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## Contacts

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# Department of Justice

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STATEMENT

OF

SCOTT D. HAMMOND  
DEPUTY ASSISTANT ATTORNEY GENERAL  
ANTITRUST DIVISION

BEFORE THE

COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE

TITLED

"FOLLOW THE MONEY: AN UPDATE ON STIMULUS SPENDING, TRANSPARENCY  
AND FRAUD PREVENTION"

PRESENTED ON

SEPTEMBER 10, 2009

STATEMENT OF SCOTT D. HAMMOND  
DEPUTY ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION  
U.S. DEPARTMENT OF JUSTICE  
BEFORE THE  
COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS  
UNITED STATES SENATE  
SEPTEMBER 10, 2009

Chairman Lieberman, Ranking Member Collins, and Members of the Committee, thank you for the invitation to provide you with written testimony discussing the proactive efforts of the Department of Justice to protect stimulus funds provided for by the American Recovery and Reinvestment Act of 2009 (Recovery Act) from fraud, waste and abuse.

With the passage of the Recovery Act, the federal government is engaging in substantial spending on needed goods and services to stimulate the economy. The language of the Recovery Act reinforces the clear mandate of the American public that those who act on their behalf to revive the economy with these funds do so responsibly and in a manner always consistent with the best interest of the public. Fraud, waste, and abuse of these stimulus funds will not be tolerated. President Obama and Vice President Biden have publically reinforced this message repeatedly. The Recovery Act represents an unprecedented, critical effort to support the American economy, and we take seriously our duty to protect that public investment. The Department of Justice is engaged in a broad effort to uphold the American public's expectation that our nation's costly investment in economic recovery will not fall victim to fraud, waste and abuse.

The Department of Justice is assisting federal, state, and local agencies in preparing to prevent, detect, and report fraudulent conduct aimed at unlawfully profiting from Recovery Act funds. The Antitrust Division is an important part of this effort. My testimony will provide a general overview of the Department's Recovery Act efforts, and highlight an initiative by the Antitrust Division to prepare procurement and grant officials to detect and report collusive and fraudulent conduct aimed at restraining competition for Recovery Act funds.

**I. Overview of the Department of Justice Initiative to Protect Recovery Act Funds**

The current financial crisis and government recovery effort requires a coordinated, proactive law enforcement response that draws on all the resources of the federal government. The Department of Justice is marshaling its criminal and civil enforcement resources to (i) investigate and prosecute these cases; (ii) recover stolen funds for victims; (iii) address issues of competition and discrimination in the use of recovery funds; and (iv) train prosecutors, agents, and private sector partners in how to detect and prevent emerging fraud schemes. We intend to draw on all the resources and expertise of the Department, together with our partner agencies and regulatory authorities throughout the Executive Branch to ensure that taxpayer funds are safeguarded from fraud and abuse and that the recovery effort is conducted in an open, competitive and non-discriminatory manner.

Given the substantial amount of funds provided by the Recovery Act, there is the potential for an increase in procurement and grant fraud at the federal and state levels. The Justice Department—through the Criminal, Civil, and Antitrust Divisions, the U.S. Attorneys' Offices, and the FBI—is prepared to play a major role in investigating and prosecuting fraudulent activities and public corruption relating to Recovery Act funding. Indeed, the Department has an established model for addressing procurement fraud targeting government funding in a consolidated, coordinated, and collaborative fashion. The model draws upon prior experiences and lessons learned from the Department's National Procurement Fraud Task Force (NPFTF).

The NPFTF, chaired by the Assistant Attorney General for the Criminal Division, was created in 2006 to promote the prevention, early detection, and prosecution of procurement fraud. Procurement and grant frauds are similar offenses to those that we are likely to see under the Recovery Act—that is, where contractors, sub-contractors, or recipients of government assistance commit fraudulent conduct in obtaining or using such funds. The Task Force is designed to leverage the resources of the Federal law enforcement community by partnering with the IGs and other law enforcement agencies. The NPFTF focuses on civil and criminal enforcement where it has the greatest effect, including defective pricing, product substitution, misuse of classified and procurement-sensitive information, false claims, grant fraud, labor mischarging, fraud involving foreign military sales, ethics and conflict of interest violations, bid rigging, and public corruption associated with procurement fraud.

The Task Force efforts have resulted in significant accomplishments, including the following:

- The Department—in coordination with the IG community—has recovered more than \$362,000,000 in civil settlements or judgments arising from procurement fraud matters;
- The Department has brought charges in hundreds of civil and criminal procurement cases since the inception of the Task Force;
- The Task Force significantly increased training for IG agents, auditors, and prosecutors regarding the investigation and prosecution of procurement fraud cases; and
- The Task Force proposed modifications to the Federal Acquisition Regulation (FAR) that significantly improved government efforts to reduce fraud in government contracts.

It should be noted that the Task Force's efforts focused exclusively on federal procurement contracts and did not address grants awarded with financial assistance, which represent a significant portion of funding under ARRA. Working in close partnership with Earl Devaney, Chairman of the Recovery Accountability and Transparency Board (the Recovery Board), and the member IGs, the Department can build upon the NPFTF model to expand efforts in the fight against Recovery Act fraud. Through such enhanced efforts, the Department aims to:

- Assess existing government-wide efforts to combat financial fraud and work with investigators, prosecutors, and regulators to ensure that financial frauds are promptly reported and addressed;
- Increase and accelerate civil and criminal prosecutions and administrative actions to recover ill-gotten gains resulting from financial fraud;
- Educate and inform the public about financial fraud;
- Increase coordination and strengthen partnerships among all law enforcement, investigative, and regulatory agencies to fight financial fraud more effectively; and
- Identify and remove barriers to preventing, detecting, and prosecuting financial fraud.

In furtherance of these goals, the Department worked closely with the Senate Judiciary Committee on the recently enacted Fraud Enforcement and Recovery Act (FERA) to amend the major frauds statute, 18 U.S.C. § 1031, to include fraud involving funds made available under the Recovery Act and the Troubled Assets Relief Program (TARP), including "any grant, contract, subcontract, subsidy, loan, guarantee, insurance or other form of Federal assistance." This amendment will ensure that Federal prosecutors have jurisdiction to use a potent fraud statute to protect the government assistance provided during this most recent economic crisis, including money from TARP, the Recovery Act, and other rescue and stimulus government assistance packages. The Department has been providing training to the IG community on the new amendments and their role in strengthening the government's ability to combat Recovery Act fraud, and working with the Recovery Board to ensure that matters are referred to the Department in a timely matter.

The FBI is actively involved in investigating potential fraud and public corruption involving Recovery Act funds. It is working closely with its law enforcement partners on the federal, state, and local level to combat Recovery Act corruption and fraud, as well as providing training and assistance to local law enforcement to monitor the use of government funds. The FBI will aggressively investigate allegations of public officials using Recovery Act funds for personal gain. Through the FBI Directorate of Intelligence and FBI Field Intelligence Groups, the FBI has increased staffing dedicated to providing both tactical and strategic intelligence relating to Recovery Act corruption and fraud. The FBI is increasing its emphasis on government fraud investigations, including fraud relating to the Recovery Act. In addition, the FBI has instituted a training initiative to provide FBI Special Agents and Intelligence Analysts an increased understanding and awareness of stimulus funding and its vulnerability to corruption and fraud. Finally, the FBI is using its community relations and liaisons to increase public awareness and encourage reporting of Recovery Act corruption and fraud.

The Civil Division also plays a major role in redressing fraud on the public treasury and is prepared to do the same with Recovery Act funds. Through enforcement of the False Claims Act (FCA), 31 U.S.C. §§ 3729-3733, the Civil Division's Commercial Litigation Branch has recovered an average of \$2 billion per year over the last six years. Since 1986, when the FCA was substantially amended, it received more than \$22 billion on behalf of federal agencies that have been victims of fraud. This statutory authority gives DOJ the ability to fight fraud as it

arises, and will allow us to prosecute fraud cases that stem from the Recovery Act that are referred to us by the IGs. In addition, the Civil Division historically has worked closely with many of the agencies receiving Recovery Act funds in combating fraud on their programs. This includes those agencies receiving the largest disbursements under the Recovery Act, such as the Department of Education, the Department of Health and Human Services, and the Department of Transportation.

In addition to suits initiated by DOJ, private plaintiffs—known as “relators” or “whistleblowers”—can bring lawsuits on behalf of the United States under the *qui tam* provisions of the FCA, and the government can intervene in appropriate cases to pursue litigation and a recovery. The Civil Division is currently receiving on average between 300 and 400 newly filed *qui tam* cases per year, and approximately 6,400 *qui tam* suits have been filed since 1986, yielding recoveries of more than \$14 billion during that period. The FCA’s *qui tam* provisions have proven to be an effective inducement for insiders to disclose wrongdoing, and they provide a potentially potent vehicle for combating fraud involving funds authorized by the Recovery Act.

Another way the Department can assist in recovering funds fraudulently obtained under the Recovery Act is through its authorization powers under the Program Fraud Civil Remedies Act (PFCRA), 31 U.S.C. §§ 3801-3812. Under PFCRA, the Assistant Attorney General for the Civil Division may authorize an agency to institute proceedings targeting false statements or claims where the damages do not exceed \$150,000. The Civil Division has been consulting with the IG community and the NPFTF on how to best use this statute to protect Recovery Act funds.

Combining all of these existing and planned efforts, the Department is marshaling and deploying its broad and diversified resources and expertise to meet the public’s expectation that the government will take all necessary steps to protect Recovery Act funds from fraud, waste, and abuse.

## **II. The Antitrust Division’s Recovery Act Initiative**

While prosecution of fraud, waste, and abuse is crucial, prevention is also an essential component of our strategy to protect government resources. As part of the broad efforts by the Department to contribute to the responsible stewardship of stimulus funds, the Antitrust Division quickly pledged its commitment to assist federal, state, and local agencies in ensuring that prophylactic measures are in place to insulate procurement and program funding processes from

bid-rigging and other antitrust violations fraudulent conduct, as well as to ensure that those who seek to corrupt the competitive bidding process are prosecuted to the fullest extent of the law. To this end, the Antitrust Division launched an Economic Recovery Initiative (Recovery Initiative) aimed at training government officials to prevent, detect, and report efforts by parties to unlawfully profit from the stimulus awards before those awards are made and taxpayer money is wasted.

The Antitrust Division investigates and prosecutes as procurement fraud schemes to undermine competitive bidding for government and commercial awards. The Antitrust Division has prosecuted these violations in a range of industries – everything from road building, to military hardware and fuel supplies, to sales of milk to public schools. The Division's experience battling such offenses has taught us that when lucrative government contracts are at stake and need to be disbursed quickly, the potential risk of collusion and fraud increases dramatically. Importantly, however, these experiences have also taught us that these risks can be dramatically minimized when an early and strong emphasis is placed on prevention and detection.

The Antitrust Division quickly mobilized to develop and implement its Recovery Initiative. The Recovery Initiative is designed to supplement and support the fraud prevention and detection efforts of the Recovery Board, the broad community of IGs for the numerous federal, state, and local agencies, and various state authorities, all of whom are principally responsible for oversight of Recovery Act funds. We ensured that the Recovery Initiative was up and running just one month after the Recovery Act was signed into law on February 17, 2009, so that the public would receive the maximum benefit of these fraud prevention and detection efforts before stimulus money was awarded.

#### **A. "Red Flags of Collusion" Training**

A key component of the Antitrust Division's Recovery Initiative is training agency procurement and grant officials, auditors, and investigators at the national, regional, and local levels on techniques for identifying "red flags of collusion" *before* the award of Recovery Act funds. This training teaches procurement and grant officials to identify collusion warning signs through case illustrations and a four-step analytical process we call M.A.P.S.

The M.A.P.S. analysis teaches individuals to look for particular indicators as they assess four categories of information in connection with awarding a procurement or grant:



MARKET – Trainees are taught to look for indicators of collusion as they determine how many vendors one would expect to compete for the award and which vendors are best positioned to perform the award.

APPLICATIONS – Trainees are taught to closely examine the proposals or applications submitted by the competing vendors and to look for suspicious similarities.

PATTERNS – Trainees are taught to review the outcome of prior awards for the same product or service to identify suspicious bidding and award patterns over time.

SUSPICIOUS BEHAVIOR – Trainees are taught to keep an eye out for suspicious behavior that indicates vendors may have colluded rather than competed for the award.

If they discover any one or a combination of indicators (or “red flags”) in these categories, procurement and grant officials are taught to report those findings to their IG office, the Antitrust Division, or other appropriate authority. Regardless of where an individual is in the spectrum of the procurement or grant process, the M.A.P.S. analysis has proven to be a simple, yet effective tool to uncover indicators that parties are attempting to collude, or have colluded, to defraud the government on a contract or grant award.

#### **B. Partnering with the IG Community and State Authorities**

For prevention and detection efforts to be most effective, they must focus equally on training government procurement and grant officials to prevent, detect, and report both “pre-award” and “post-award” indicators. The “red flags of collusion” training offered by the Antitrust Division focuses on pre-award collusion indicators – indicators that arise before a government award is made. Post-award fraud awareness training programs offered by the Department will focus on illegal conduct that occurs after a government award is made, such as fraudulent charges to the government for manpower or materials that were not performed or used in the completion of the government project. Thus, as part of our Recovery Initiative, we are working with the Criminal Division to partner with the IG community and state authorities to combine our pre-award fraud training program with the traditional post-award fraud training provided by those offices.

Since the inception of the Initiative in March 2009, the Antitrust Division has had tremendous success in partnering with the broad network of IGs for the numerous federal, state, and local agencies and state authorities who are overseeing the distribution of Recovery Act funds. We approached these agencies with an offer to help train IG agents and auditors on pre-

award fraud indicators and then to partner with those same agents and auditors to develop a strategy to jointly conduct pre- and post-award fraud awareness briefings for their agency procurement and grant officials. Not surprisingly, given the significant challenge facing the IG community and states to oversee the proper handling of Recovery Act funds, our offer to assist has received an overwhelmingly positive response.

1. *Partnering with Federal Agencies*

On the federal level, the Antitrust Division has worked closely with the Recovery Board and the entire network of IGs for the federal agencies. To date, we have conducted or scheduled training presentations with 18 federal agencies receiving Recovery Act funds, including: Department of Agriculture, Department of Commerce, Department of Defense, Department of Education, Department of Energy, Department of Health and Human Services, Department of Homeland Security, Department of Housing and Urban Development, Department of the Interior, Department of Justice, Department of State, Department of Transportation, Department of the Treasury, Department of Veterans Affairs, Environmental Protection Agency, General Services Administration, National Aeronautics and Space Administration, and Small Business Administration. The Department of Justice is coordinating with the Vice President's Recovery Implementation Office on the risk management program already mandated at ARRA funded agencies.

With the IG offices for those agencies receiving the largest volume of Recovery Act funding, we have developed national strategies to partner on pre- and post-award fraud awareness training for agency procurement and grant officials nationwide. For example, working in partnership with the IG Office for the Department of Transportation (DOT OIG), the Antitrust Division and DOT OIG provided comprehensive fraud awareness training to the entirety of the more than 70 regional offices and over 2,600 employees of the Federal Highways Administration via webcast. We have also been conducting joint, in-person training sessions with DOT OIG around the country for other components of the Department of Transportation, such as the Federal Aviation Administration. Another example of these partnerships in action is the Antitrust Division's work with the IG Office for the Department of Commerce (DOC OIG). To date, the Antitrust Division and DOC OIG have conducted over 20 joint, in-person training sessions around the country for over 350 procurement and grant officials in Commerce's various components.

The Antitrust Division has not, however, limited its attention to just those agencies receiving the most sizeable Recovery Act funding. We have also partnered with the IG offices of federal agencies receiving more modest Recovery Act funding to provide individual training to all of those persons who will be specifically handling Recovery Act funds. One such agency is the Department of Veterans Affairs (VA). In conjunction with the IG Office for the VA, the Antitrust Division has, to date, provided three training programs to over 200 VA agents and procurement officials stationed around the country.

2. *Partnering with the States*

On the state level, we are working with the National Association of Attorneys General (NAAG) and National Governors Association (NGA). In coordination with the NAAG and NGA, we are working closely with appointed state Recovery Czars and state IG and attorney general offices to coordinate training for procurement and grant officials who will be distributing Recovery Act funds at the state and local levels. We have already held or scheduled antitrust training programs for 23 states and we are working to schedule training programs with the remaining states. The states we have worked with thus far are: Alaska, Arizona, Arkansas, California, Florida, Georgia, Hawaii, Idaho, Kentucky, Maryland, Montana, New Jersey, New York, Montana, Ohio, Oregon, Pennsylvania, Texas, Utah, Virginia, Washington, Wisconsin, and Wyoming. We have also conducted training presentations for the territory of Guam.

In addition to providing training to the states, we have played a significant role in assisting states in their efforts to coordinate comprehensive bid-rigging and related fraud training programs that mirror the programs we provide in partnership with IG offices at the federal level. Providing such comprehensive training programs at the state level requires far more coordination among various federal and state components to ensure that a training program covers all appropriate topics, but also does not result in any wasteful overlap of efforts. Given the advanced stage of our Recovery Initiative, we have been able to assist states in the very important role of coordinating these comprehensive training programs. For example, in California, the Antitrust Division worked with the members of the Western Region IG Council and the U.S. Attorney's Office for the Eastern District of California to develop a comprehensive training presentation to California state compliance review officers, procurement and grant officials, auditors, investigators, and department heads. The training included representatives

from multiple agencies who covered pre- and post-award fraud training, as well as various other topics related to oversight of Recovery Act funds.

*3. These Partnerships Are Producing Results*

As a result of our federal, state, and local efforts to date, the Antitrust Division has already conducted nearly 250 training presentations. Through those presentations, we have trained over 13,000 agents, auditors, and procurement and grant officials nationwide. We are scheduled to train thousands of additional procurement and grant officials in the next few months.

**C. Troubleshooting Procurement and Program Funding Processes**

Beyond our work with the investigative arms of the various agencies and states, our Recovery Initiative sets as a goal connecting our competition experts with agency program, procurement, and grant officials to begin a dialogue about “best practices” agencies may adopt to protect their procurement and program funding processes and to maximize open and fair competition. While we consider this aspect to be a long-term goal of the Recovery Initiative, the Antitrust Division has already been invited to join federal and state agencies in brainstorming ways to further protect their proposed procurement processes for use of Recovery Act funds. For example, the Division was invited to meet with representatives from the Department of Commerce’s Recovery Act Task Force to discuss the National Telecommunications and Information Administration’s (NTIA’s) Broadband Technology Opportunities Program (BTOP). Specifically, the Division was invited to advise the Task Force about the types of collusion and fraudulent schemes that may be employed to target BTOP funds. The Division provided insights to the Task Force on this issue based on its successful investigation and prosecution of collusion and fraudulent schemes used to target an existing government program with a structure similar to that envisioned for the BTOP.

**D. Criminal Enforcement**

The Department has further solidified its relationships with the various federal and state IG offices and state authorities. These relationships will prove to be critically important when preventive mechanisms fail to adequately protect Recovery Act funds from collusion or fraud, as these agencies and states will know that the Department is here to help them investigate and prosecute any criminal conduct directed at thwarting competition for those funds.

**E. Public Outreach**

Understanding that the public often serves as the best check and resource for identifying fraud, waste, and abuse of government funds, the Antitrust Division has invited the public to learn more about, and participate in, making the Recovery Initiative a success. Information about the Recovery Initiative is available to the general public on the Department of Justice web site at: [http://www.usdoj.gov/atr/public/criminal/economic\\_recovery.htm](http://www.usdoj.gov/atr/public/criminal/economic_recovery.htm). This web site provides the public with information about how to detect possible antitrust violations in connection with Recovery Act funds, including a printable version of the "Red Flags of Collusion" desk reference the Division distributes at training presentations and which agencies have incorporated into publication materials they send to Recovery Act fund recipients. The web site also provides the public with contact email addresses to use to report Recovery Act-related complaints, as well as to request collusion awareness training. A description of the Recovery Initiative and a link to the Antitrust Division web site is also available to the public on the official Recovery Act web site – [www.recovery.gov](http://www.recovery.gov).

**III. Conclusion**

The Department of Justice is committed to deterring fraudulent and criminal conduct aimed at undermining the government's procurement processes and the economy at large, through swift and just prosecutions. We appreciate the leadership of the President and the Vice President in calling for continual and vigilant oversight of ARRA spending. The Department's broad proactive efforts to protect Recovery Act funds, through the Antitrust Division's Recovery Initiative and other efforts, demonstrate the Department's equally important commitment to providing government officials the tools they need to prevent and root out these forms of fraudulent and criminal conduct before that conduct results in a single dollar of loss to the American taxpayer.

**Request for information to the Honorable Robert L. Nabors II  
From Senator Roland W. Burris**

**“Follow the Money: An Update on Stimulus Spending, Transparency, and Fraud Prevention”  
September 10, 2009**

Q: What are the numbers you have pertaining to stimulus funds for minority owned small businesses and/or minority contractors? I am requesting Hispanic and black numbers specifically, but any numbers relating to minorities in general would be exactly what we are looking for.

A: The Small Business Administration provided the numbers below, using information provided by small businesses in contracting databases, which include Recovery Act Funding.

Data as of October 6<sup>th</sup>:

Minority Owned Small Business - \$1.82B (11.4%)  
Small Disadvantaged Business - \$1.69B (10.6%)  
Black Owned - \$291.99M (1.8%)  
Hispanic Owned - \$484.82M (3.1%)

Note:

SBA relies on firms to self-identify themselves. There is no verification or validation of this particular information.

**Request for information to the Honorable Robert L. Nabors II  
From Senator Tom A. Coburn**

**“Follow the Money: An Update on Stimulus Spending, Transparency, and Fraud Prevention”  
September 10, 2009**

Q: In your testimony, you said that each of the stimulus projects is carefully reviewed by OMB to ensure that their uses of Recovery Act funds are thoughtful and appropriate. You work with agencies to identify and revise projects that do not meet that threshold. Could you make the list of those projects that you have identified and revised available to the committee?

A: The office of Management and Budget (OMB) remains committed to monitoring implementation and tracking projects that receive funding. OMB has issued multiple rounds of guidance and participated in a variety of forms of outreach to reporting entities, explicating reporting requirements and providing clarification to questions received from those reporting.

Several stages of review occur before Recovery Act funding is awarded to an entity. Federal agencies thoroughly examine proposals, which often undergo several layers of review even within an agency. Additionally, OMB reviews lists provided by agencies before any funding is obligated. The Office of Management and Budget does not keep a comprehensive list of projects that did not receive funding during OMB review or agency review.

Below is a list of proposed projects which have not received funding after Administration examination.

**Department of Defense (DOD)**

The DOD removed 16 projects from their final project lists during internal discussions. Projects involved the following types of activities:

- Three projects to renovate swimming pools.
- Nine projects to renovate, repair, or upgrade various athletic facilities such as basketball or tennis courts.
- A project to repair and/or straighten headstones at a cemetery.
- A project to steam-clean bird droppings from a building.
- A project to repair the roof of a fast food franchise on a military base.
- A project to renovate a historic district on a military base.

**Army Corps of Engineers (ACOE)**

The ACOE removed or modified three projects from their final project list:

- A project to install a guardrail at Lake Optima in Oklahoma was modified to instead demolish abandoned campground facilities.
- A project to print pamphlets for a Lake Onondaga restoration project was modified from printing paper pamphlets to publishing the information online.
- A project in the Everglades was deferred due to being a “new start.” (New starts are prohibited by the Act).

**Department of Transportation (DOT)**

The DOT worked with states to remove or modify nine projects from their proposed lists.

- A state DOT planned to use funds to resurface a road. Subsequent to that project, an EPA remediation project was planned that would have multiple heavy trucks hauling waste across the newly laid road – most likely severely damaging the road in the process. The DOT project has been rescheduled and will be reinstituted after the EPA project is complete.
- A state DOT planned to spend \$57 million on road planning studies, rather than shovel-ready projects. After discussions with DOT, the state is now using the funding for road construction projects.
- A state DOT planned to spend transportation funds on a memorial project, a use that is ineligible for transportation enhancement funds.
- A state DOT planned to spend funds to develop an inventory of American with Disability Act (ADA) needs in the state. Developing such an inventory for planning and prioritization purposes is not an eligible transportation enhancement activity.
- A state DOT planned to use funds to establish a landscaping and scenic beautification program for highways located throughout the state, an activity deemed ineligible for transportation enhancement funds.
- A state DOT planned to use funds to upgrade a marina breakwater at a state park, an activity not eligible for transportation enhancement funds.
- A state DOT planned to use funds for several preliminary engineering projects for major highway improvements, without an identified funding source to complete the projects after the engineering work was complete.
- A county Transportation Authority distributed “baseline” funding to cities in the county. Some cities did not have eligible Recovery Act projects ready-to-go, and sought to trade their transportation funds, at a discount, to other cities, in return for general fund money. These trades were halted.
- A public transportation agency planned to use funds to purchase right-of-ways with no discernible immediate job creation impact, but after discussions with the Federal Transit Administration (FTA), used the funds for alternate projects.

**Department of Interior (DOI)**

During internal discussions, DOI halted or modified 12 projects, most related to water reclamation projects:

- A plan to use funds to purchase a supplemental freezer, one use of which would have been to freeze fish sperm, at the Gavin's Point National Fish Hatchery was halted.
- A plan to use funds to purchase five aircraft used to conduct migratory bird surveys was halted.
- Three cities plans to use Title XVI water reclamation funds for projects that would have provided water delivery to prohibited facilities (such as golf courses, casinos, etc.) were halted.
- An internal DOI plan to establish renewable energy coordination offices, including significant funding for employee relocation, which would handle the permitting of private-sector renewable energy projects on public lands was deemed ineligible for ARRA funding.



- DOI worked with six cities to modify water projects so that funds were not being used to deliver water to golf courses, reducing project cost and freeing up funds for other projects.

#### **General Services Administration (GSA)**

The GSA halted the following project associated with work on the Executive Offices:

- A proposal to repair and rehabilitate the East Wing of the White House was halted.

#### **Department of Justice (DOJ)**

During pre-award discussions between DOJ and grant recipients, the following four grant programs were modified:

- A sheriff's office proposal to use the Recovery JAG funds to implement the "Employee Retention Program" to connect professional achievement with incentives, motivating employees to a higher potential and inspiring longevity and commitment to the department was determined to neither meet the definition of economic stimulus nor provide long-term benefits to the community.
- After discussions with DOJ, a police department decided not to use ARRA funds to purchase police lockers.
- A county proposed to spend funds for one armored vehicle, but after discussions with DOJ, opted to use funds elsewhere.
- A proposal to use funds to purchase two police cruisers for two school resource officers to drive to and from the schools to teach gang resistance programs was halted. The notion was to use the cruisers to transport materials and supplies used in the classroom instruction.

#### **Department of Agriculture (USDA)**

During internal discussions, USDA halted the following twelve projects:

- A proposal to use Rural Development Community Facilities funds for uniform service revolvers and Tazer safety guns for Sheriff Deputies was halted.
- A proposal to use Rural Development Community Facilities funds for pre-school outdoor playground equipment was halted.
- A proposal to use a Rural Development Business and Industry loan for a ski resort was halted.
- A proposal to use a Rural Development Business and Industry loan for a luxury spa and inn was halted.
- A proposal to use a Rural Development Business and Industry loan to refinance a drugstore was halted.
- A proposal to use a Rural Development Business and Industry loan for a gas station was halted.
- Six proposals across the country to use Floodplain Easements funds were denied as the applications were for sites that are in permanent vegetation such as grass and trees, with little evidence of flood damage and would require very limited restoration and thus, limited job creation, and did not meet program guidelines.

**Department of Labor (DOL)**

The DOL denied one proposed use of ARRA funds:

- A requester proposed using funds to rent the Georgia Superdome for an event on homelessness.

**Housing and Urban Development (HUD)**

In addition to the projects listed above for other agencies, the Department of Housing and Urban Development worked with each of their recipients of Community Development Block Grants (CDBG) to ensure that ARRA funds were used for the most appropriate types of uses, and modified approximately 116 submitted project lists. Samples of the types of projects modified are listed below:

- 48 cities submitted proposals to renovate, rehabilitate, or upgrade parks
- 52 cities submitted proposals to renovate, rehabilitate, or upgrade recreation centers, playgrounds, athletic fields, or other similar facilities
- 12 cities submitted proposals for funding to support youth –centered recreational activities
- Four cities submitted proposals for funding to build or upgrade skate parks

Funds were instead directed to infrastructure projects, housing assistance and job training centers, and sidewalk and streetlight improvements.

**Post-Hearing Questions for the Record  
Submitted to the Honorable Robert L. Nabors II  
From Senator Joseph I. Lieberman**

**“Follow the Money: An Update on Stimulus Spending, Transparency, and Fraud Prevention”  
September 10, 2009**

1. Over the July 4th weekend, several federal websites faced outages when they were subject to denial-of-service attacks. Last year, in a different type of attack, bad actors took advantage of inadequate security on popular federal websites to infect visitors with malicious software.

- a. Given the increased security risks that our information infrastructure is seeing every day, what steps has OMB taken to raise the security of both [financialreporting.gov](http://financialreporting.gov) and [Recovery.gov](http://Recovery.gov)?

*Managing the security and infrastructure of Recovery.gov and Federalreporting.gov is the responsibility of the Recovery Accountability and Transparency Board. We understand that both sites were fully certified and accredited, and that they went through extensive security testing.*

- b. Do you expect that they will be compliant with the requirements of the Federal Information Security Management Act (FISMA)?

*The Recovery Accountability and Transparency Board is responsible for making all related decisions about the FISMA compliance of both of these websites. We understand from the Board that the sites will be compliant with FISMA.*

2. In previous efforts to track government spending, there have been challenges in incorporating sub-award data. My understanding is that only the prime recipient of Recovery Act funds and sub-recipients one level below will be responsible for reporting on use of federal funds. The prime recipients will report on payments to commercial vendors and other sub-recipients, and sub-recipients also must identify vendors receiving over \$25,000.

- a) Can you explain to us how far the funds will be tracked with Recovery.gov and what the challenges there will be with getting this information?

*Per the requirements of the Recovery Act, all recipients are required to provide detailed information down to the sub-recipient level. OMB's implementing guidance gives recipients the option of delegating reporting to sub-recipients, but in either case, the prime recipient remains responsible for verifying the data. OMB's guidance also calls for recipients and sub-recipients to report on all vendors receiving more than 25,000, which will provide an additional level of detail beyond what is required by law. The Recovery Accountability and Transparency Board is responsible for making all of the*

*recipient information public on Recovery.gov, and they have determined that reports on contracts will be made public on October 15, and that reports from grant recipients will be made public on October 31. In the intermediate period between October 10 and October 31, prime recipients as well as granting agencies will be required to review the data and provide corrections in the event that they find errors. However, consistent with the statute and the Board's and OMB's shared goal of transparency, any corrections to the data will be visible to the public.*

*October recipient reporting is unprecedented in the level of detail that it demands of Federal grant and contract recipients, who have not been asked previously to report back on their use of funds with such detail. In particular, the requirement that recipients calculate the number of jobs created with Federal funds represents a new kind of analysis that recipients of Federal funding have not had to execute in the past. We are cognizant of the fact that the reporting requirements present new challenges for recipients, and we have implemented extensive support mechanisms to help them through this process. We have issued three rounds of implementing guidance, which explicate the reporting requirements, provide clarification on the approved methodologies for jobs reporting, and include detailed instructions on how to use Federalreporting.gov.*

*OMB has held over 20 training sessions—including 13 webinars for which over 17,000 participants signed up. Together, the Administration has held over 150 conference calls with recipients, over 150 events with state officials, 19 events with local government officials, and seven White House and Administration forums. In anticipation of recipient needs surrounding the October 10 deadline, OMB also worked with the Board to deploy on-site support teams to help manage the workload in State capitals and the localities that are likely to be dealing the highest volume of paperwork. These teams work closely with a Washington-based coordinating team to respond to recipient concerns and make sure that their questions are addressed, and to stay attuned to challenges that emerge so that they can be addressed for subsequent reporting periods.*

- b) Given the sheer amount of information that will be flowing into Federalreporting.gov and Recovery.gov there will be challenges in ensuring the data is accurate. Can you explain how OMB will ensure that this website is populated quickly and accurately?

*The Recovery Act tasked the Recovery Accountability and Transparency Board to manage Recovery.gov, and the Board makes all final decisions with respect to when the site is populated with recipient data. Recipients are required by law to submit their information for the first quarterly reporting period by October 10, and ultimately, the accuracy of the data will depend on their compliance with that requirement. We believe that the outreach efforts described above will help educate recipients about the nature of what they are required to report, and about the timeline for registration on Federalreporting.gov and for reporting their information.*

- c) Who is ultimately responsible for the accuracy of the data on Recovery.gov and how will they be held accountable?

*It is ultimately the responsibility of recipients, as required by law, to report accurate information. Agencies will provide an additional level of review to assist recipients with*

*data quality. Recipients who fail to report by the October 10 deadline will be contacted by a government agency to remind them they must report. Those recipients who still fail to report are subject to the terms and conditions of their Federal contract or grant, and may be subject to penalties including economic sanctions such as cancellation, suspension, or debarment. In some cases, intentional reporting of false information can result in civil and/or criminal penalties. Agencies have significant latitude in deciding how to address these situations and take into consideration a variety of factors in their decision.*

3. In June, Federal Chief Information Officer Vivek Kundra launched the IT Dashboard, which brings new visibility into IT spending across the federal government. The website is updated monthly and tracks how well contractors are meeting their cost and schedule requirements. Do you think there would be value in including Recovery.gov on the Federal IT Dashboard, so that citizens can track performance data?

*Currently, the IT Dashboard is populated by data from 28 major executive agencies that have historically reported on their major information technology investments in the Information Technology (IT) Portfolio Report (Exhibit 53 of OMB Circular A-11). Small and independent agencies have not been required to submit these reports, but they have been encouraged to do so at their discretion for investments that merit greater transparency. Because the Recovery Accountability and Transparency Board is an independent entity, it is not required to submit this information.*

**Post-Hearing Questions for the Record  
Submitted to the Honorable Robert L. Nabors II  
From Senator Robert F. Bennett**

**“Follow the Money: An Update on Stimulus Spending, Transparency, and Fraud  
Prevention”  
September 10, 2009**

1. Mr. Nabors, shortly before the recess Congress passed a \$2 B offset for the cash for clunkers shortfalls using \$2 B in stimulus funds provided for loan guarantees provided to renewable energy project and transmission infrastructure.

While, I believe it was appropriate to offset any new spending, I am concerned that the Administration has committed repay this funding further adding to the deficit. Can you tell me if the Obama Administration has committed to repay this funding and increase the deficit?

*The Successful Cash for Clunkers program was supported by redirecting funds appropriated to the Title XVII renewable energy loan guarantee program at the Department of Energy. The Department was not expected to use those funds immediately. At that time, the President committed to replenishing the funding for this important loan guarantee program that will advance new energy technologies and increase the supply of renewable energy. We are currently working with the relevant Congressional committees to identify the appropriate offset.*

**Post-Hearing Questions for the Record  
Submitted to the Honorable Earl E. Devaney  
From Senator Joseph I. Lieberman**

**“Follow the Money: An Update on Stimulus Spending, Transparency, and Fraud  
Prevention”  
September 10, 2009**

1. You testified on September 10<sup>th</sup> that more than 17,000 recipients had registered on the federalreporting.gov website. This only represents a sliver of the number of overall recipients, given that approximately 200,000 individuals will need to file reports by October 1st. This will create considerable demands on the site's infrastructure. Similarly, it is likely that Recovery.gov will also face a similar increase in October once the additional data and functionality is added. This increased demand may lead to service problems, just as the public had difficulties accessing Grants.gov and Cars.gov during high-demand periods earlier this year.
  - a. Given these incidents, what sort of testing is the Recovery Board doing to ensure both websites are capable of meeting the anticipated spikes in demand around the initial reporting deadline?

*Extensive preproduction performance testing was completed on both the Recovery.gov and FederalReporting.gov websites. Different scenarios were employed to simulate the registration process and the report submission process for an estimated 150,000 users. For the Recovery.gov website, both geospatial and data searches were executed, and server response time was measured. Based on results, some infrastructure adjustments were made to allow for greater bandwidth transmissions, resulting in improved performance and response times.*

*During the actual registration and report submission timeframes, the system performed well and was able to respond to spikes throughout the submission period. The FederalReporting.gov system was available for the entire reporting period, and there were no unanticipated server outages or application failures.*

- b. How confident are you that both websites will have adequate input, storage, and processing capacity to respond to the recipient reporting period that begins on October 1?

*The FederalReporting.gov database and server storage space were sized with ample capacity to meet the anticipated storage requirements for this first submission, as well as subsequent cumulative reporting each quarter. The data will then be transferred and posted on the Recovery.gov website for public consumption. In anticipation of the high demand to download the raw data file in its entirety, we will leverage the cloud computing environment implemented for the Recovery.gov site, minimizing actual hits and queries on the server.*

2. Over the July 4th weekend, several federal websites faced outages when they were subject to denial-of-service attacks. Last year, in a different type of attack, bad actors took advantage of inadequate security on popular federal websites to infect visitors with malicious software.
  - a. Given the increased security risks that our information infrastructure is seeing every day, what steps has the Board to raise the security of both financialreporting.gov and Recovery.gov?

*The Board has implemented information security controls commensurate with the categorization and sensitivity of the information being stored, transmitted, and presented. Prior to production, both Recovery.gov and FederalReporting.gov information security controls were certified to determine if they were implemented correctly, operating as intended, and producing the desired outcome with respect to meeting the security requirements for each system. Using the guidance provided by NIST SP 800-37, both Recovery.gov and FederalReporting.gov were authorized to operate as required by FISMA.*

- b. Do you expect that they will be compliant with the requirements of the Federal Information Security Management Act (FISMA)?

*Yes. In conducting the security certification and accreditation process, FISMA protocol was followed, including the development of a security plan, security assessment report, plan of actions and milestones, an independent audit, and testing.*

3. You testified at our hearing that Recovery.gov “will lay the groundwork for how future government spending is tracked.” In previous efforts to track government spending, there have been challenges in incorporating the sub-award data. Only the prime recipient of Recovery Act funds and sub-recipients one level below will be responsible for reporting on use of federal funds. The prime recipients will report on payments to commercial vendors and other sub-recipients, and sub-recipients also must identify vendors receiving over \$25,000.



- a. Can you explain to us how far the funds will be tracked with Recovery.gov and what the challenges there will be with getting this information?

*The Office of Management and Budget (OMB) is responsible for policy-based decisions on the specific levels of recipient reporting. Guidance issued by OMB on June 22, 2009, stated that Recovery.gov would track funds at the prime recipient level, the subrecipient level, and – in the case of vendors receiving more than \$25,000 – the vendor level.*

*It is difficult to be aware of the full extent of any challenges in obtaining the recipient information at this early stage. Extensive communications and outreach were employed by the Board to educate recipients throughout the country. These efforts ranged from recorded webinars to conferences to the High Volume Coordinator program, the help desk and coordination with every major state and local association.*

- b. Given the sheer amount of information that will be flowing into Federalreporting.gov and Recovery.gov there will be challenges in ensuring the data is accurate. How will the Board ensure that this website is populated quickly and accurately?

*It is the responsibility of the federal agencies to develop internal policies and procedures for reviewing reported Recovery Act data. However, the Board has developed a Data Quality Review Guide. The Data Quality Review Guide was prepared for Inspectors General to review what processes an agency is using to review Section 1512 data submitted by Recovery Act fund recipients.*

*It is the Board's responsibility to ensure that the data on Recovery.gov is a true reflection of what recipients report, including any subsequent modifications made to that data. The Board has conducted extensive end-to-end testing using a control data set to verify the integrity of the information being entered into FederalReporting.gov through to the output displayed on Recovery.gov.*

The following schedule and process for displaying recipient data on [www.recovery.gov](http://www.recovery.gov) have been established:

- All reported data associated with Recovery contracts awarded directly by federal agencies will be displayed by Oct. 15.
- All reported data associated with Recovery grants, loans and other forms of assistance will be displayed on Oct. 30.
- All data changes made by recipients between Oct. 11 and Oct. 29 will be carefully tracked, chronicled, and made available on Recovery.gov shortly after Nov. 1.

- c. Who is ultimately responsible for the accuracy of the data on Recovery.gov and how will they be held accountable?

*The award recipients who file reports in accordance with section 1512 of the Recovery Act are ultimately responsible for the accuracy of their data. The FederalReporting.gov system allows agencies to flag data accuracy issues, but only recipients can change their data. Agencies are responsible for establishing their own internal review processes, and, if during its review an agency discovers data accuracy issues, it is the responsibility of the agency to coordinate and resolve report submissions with the recipients. OMB has assumed the lead for establishing data quality standards.*

*Although the Recovery Act itself prescribes no legal sanctions for incorrect or omitted data, potential penalties for inaccurate, false, or misleading data range from administrative (termination of award or adverse past-performance evaluations for non-compliant contractors) to civil (application of the newly expanded Civil False Claims Act) to criminal (the false statements statute).*

4. Given the interest in Recovery.gov, how is the Board bringing in stakeholders to discuss the features they would like to see on the website?

*Prior to the launch of Recovery.gov 2.0, the Board began an extensive outreach effort to gain feedback from the various stakeholder communities. In April, the Board launched the first in a series of outreach efforts with the public, holding an electronic forum for website development ideas. The Board also initiated regular meetings with senior contract and grant officials in federal agencies responsible for disbursing Recovery funds and began consulting with local and state oversight officials.*

*The first online forum conducted April 27-May 3, 2009, resulted in 22,000 visitors from 50 states and 98 foreign countries, including Fortune 500 companies and small businesses, web designers and financial services experts, internet novices and the creators of the World Wide Web and Web 2.0. The week-long national web-based "town hall" was intended to obtain innovative ideas from the public to integrate, track, and display data from thousands of federal, state, and local entities. The Board partnered with the National Academy of Public Administration to execute the event.*

*A series of additional webinars, conference calls, and on-site visits with key stakeholders and the public were conducted in August and September prior to the launch of the Recovery.gov 2.0 website. Participants were presented with proof of concept for a new Recovery website and were asked for input on usability and relevance. These outreach efforts included stakeholders from Dayton, Ohio; Boston, Massachusetts; Dallas, Texas; Sacramento, California; and Richmond, Virginia. In addition, presentations have been given to the Vice President and OMB, congressional leaders, the press, and the Inspector*

*General community. Watchdog groups such as the Sunlight Foundation and OMB Watch were also conducted.*

5. In June, Federal Chief Information Officer Vivek Kundra launched the IT Dashboard, which brings new visibility into IT spending across the federal government. The website is updated monthly and tracks how well contractors are meeting their cost and schedule requirements. Do you think there would be value in including Recovery.gov on the Federal IT Dashboard, so that citizens can track performance data?

*The Board currently posts monthly financial reports including program performance and cumulative activities on the Recovery.gov website. While the IT Dashboard tracks major IT expenditures by agencies, Recovery.gov is the government's sole official site for tracking performance regarding Recovery Act funds. OMB has informed the Board that the Board is not required to submit such IT information for inclusion on the IT Dashboard.*

